

See discussions, stats, and author profiles for this publication at: <https://www.researchgate.net/publication/281119463>

Kamardin et al (2014) Board diversity MDIR OS & FP Prosiding MIICEMA

Data · August 2015

CITATIONS

0

READS

1,921

4 authors:



Hasnah Kamardin

Universiti Utara Malaysia

78 PUBLICATIONS 612 CITATIONS

[SEE PROFILE](#)



Rohaida Abdul Latif

Universiti Utara Malaysia

58 PUBLICATIONS 275 CITATIONS

[SEE PROFILE](#)



Kamarun Nisham Taufil Mohd

Universiti Utara Malaysia

66 PUBLICATIONS 253 CITATIONS

[SEE PROFILE](#)



Noriah Che Adam

Universiti Utara Malaysia

23 PUBLICATIONS 117 CITATIONS

[SEE PROFILE](#)

Some of the authors of this publication are also working on these related projects:



IPO Valuation [View project](#)



FINANCIAL DISTRESS AND RESTRUCTURING OUTCOMES IN MALAYSIA [View project](#)



miicema

Malaysia Indonesia International Conference on
Economics, Management and Accounting

MIICEMA 2014

CONFERENCE PROCEEDINGS

Global Economic Climate: Issues and Challenges

Hotel Bangi-Putrajaya,
Malaysia

10 - 11 November
2014

ISBN 978-983-3198-82-5



9 789833 198825



MIICEMA 2014 ORGANISING COMMITTEE

Committee Members

Patron: Professor Datuk Dr Noor Azlan Ghazali

Advisors: Professor Dr Nor Ghani Md Nor

Associate Professor Dr Maisarah Ahmad

Chairperson: Dr Mohd Rizal Palil

Co-chairperson: Lt Cdr (Retd) Dr Lokhman Hakim Osman

Secretary: Miss Normaziah Zaini

Finance: Dr Mara Ridhuan Che Abdul Rahman

Marketing and Publicity: Dr Norlin Khalid

Protocol and Reception: Dr Mohd Mohid Rahmat

Working Papers and Publication: Associate Professor Dr Hawati Janor

Certificates and Souvenirs: Associate Professor Dr Mariani Abdul Majid

Logistics: Mr Mohd Dzul Azzwan Mohd Nor

Technical and Special Tasks: Dr Hazrul Izuan Shahiri

Website and Technology: Dr Khairul Azman Aziz

Keynote Speaker and VIP Invitation: Associate Professor Dr Noorasiah Sulaiman

Sub-Committee Members

Associate Professor Dr. Mohd. Azlan Shah Zaidi

Associate Professor Dr. Nor Liza Abdullah

Dr. Abu Hanifah Ayob

Dr. Amizawati Mohd. Amir

Dr. Mohd. Hasimi Yaacob

Dr. Rozita Amiruddin

Mr Hairunnizam Wahid

Miss Siti Ngaesah Ab. Hamid

Miss Veelaiporn Promwichit

Mr Muhammad Shah Rizal b. Mohd. Ghazali

Mrs Haslina Hamdan

Miss Hasni Arshad

Mr Muhamad Azrin Supar

Mr Mohammad Zukry Ahmad

Mrs Noorsyam Noordin

Miss Nor Nadia Nordin

Mrs Norul Syuhada Abu Hassan

Miss Nadzirah Yahya

PANEL PENILAI / PANEL OF REVIEWERS

Professor Dr. Ishak Yussof
Professor Dr. Norman Salleh
Professor Dr. Rahmah Ismail
Associate Professor Dr. Aini Aman
Associate Professor Dr. Aisyah Abdul Rahman
Associate Professor Dr. Azhar Ahmad
Associate Professor Dr. Azman Ismail
Associate Professor Dr. Basri Abdul Talib
Associate Professor Dr. Che Aniza Che Wel
Associate Professor Dr. Doris Padmini Selvaratnam
Associate Professor Dr. Hawati Binti Janor
Associate Professor Dr. Madeline Berma
Associate Professor Dr. Maisarah Ahmad
Associate Professor Dr. Mariani Abdul Majid
Associate Professor Dr. Mohamat Sabri Hassan
Associate Professor Dr. Mohd Azlan Shah Zaidi
Associate Professor Dr. Mohd Hizam Hanafiah
Associate Professor Dr. Nor Asiah Omar
Associate Professor Dr. Nor Liza Abdullah
Associate Professor Dr. Norazlan Alias
Associate Professor Dr. Norlida Hanim Mohd Salleh
Associate Professor Dr. Romlah Jaafar
Associate Professor Dr. Rosmah Mat Isa
Associate Professor Dr. Ruhanita Maelah
Associate Professor Dr. Ruzita Abdul Rahim
Associate Professor Dr. Shahida Shahimi
Associate Professor Dr. Sofiah Md Auzair
Associate Professor Dr. Syed Shah Alam
Associate Professor Dr. Zafir Mohd Makhbul
Associate Professor Dr. Zakiah Mohammaddun Mohamed
Associate Professor Dr. Zizah Che Senik
Associate Professor Dr. Zulkefly Abdul Karim
Dr. Abu Hanifah Ayub
Dr. Harlina On
Dr. Hazrul Izuan Shahiri
Dr. Hendon Redzuan
Dr. Lohhman Hakim Osman
Dr. Mara Ridhuan
Dr. Mohd Adib Ismail
Dr. Mohd Daud Ismail
Dr. Mohd Hasimi Yaacob
Dr. Mohd Rizal Palil
Dr. Noor Azryani Auzairy

Dr. Noor Azuan Hashim
Dr. Nor Hasni Juhdi
Dr. Norazila Mat
Dr. Norida Basnan
Dr. Norlin Khalid
Dr. Norsiah Aminudin
Dr. Roshayati Abdul Hamid
Dr. Rosiati Ramli
Dr. Rozita Amiruddin
Dr. Rubaayah Yaakob
Dr. Shifa Mohd Nor
Dr. Zaleha Yazid
Mr. Ahmad Raflis Che Omar
Mr. Mhd Suhaimi Ahmad
Mrs. Farhana Sidek



TABLE OF CONTENT

Quality of Human Resources and Application of Income Tax Accounting at Construction Company in Palembang City	3
Pension Fund Investment in Nigeria: Islamic Perspective.....	21
Kajian Penggunaan Tajuk dalam Penyata Kewangan di Malaysia	31
Internet Financial Reporting of Malaysian Companies - A Study of Preparers' Perception	49
Detecting Earnings Manipulation by Malaysian Public Listed Companies: The Reliability of Beneish M-Score Model.....	67
The Implementation and Disclosure of Corporate Social Responsibility (CSR) in Indonesian Banking Industries.....	82
The Effect of Internal Audit Quality on Good University Governance and its Implications on The Quality of Education Operation that Contributes to Graduates Quality: A Case Study at Private Higher Educations in Region III Of West Java Indonesia	98
The Effect of General Allocation Fund (DAU) and Regional Real Income (PAD) on the Regional Expenditures (Empirical Studies of the Government District/city of the Province of Bengkulu)	117
Determinants Company Conditions in Disclosure Corporate Social Responsibility: Case Study in High Profile Indonesian manufacturing companies.....	138
Preliminary Analysis on Related Party Transactions in Corporate Circulars	146
The investigation of the credit risk and its role in cash flows, macroeconomic factors and competition in Iranian banking industry	158
The Influencing of Local Parliaments (DPRD) Control Function on Good Government Governance (GGG) with their knowledge about budget as a moderating variable (study on local parliaments of Bengkulu Province 2009-2014).	165
Discharging Accountability through Governance: Cases from Waqf Institutions in Indonesia	181
Ownership Structure and Risk Taking of Malaysian Banking Institutions.....	193
The Effect of Disclosure Corporate Social Responsibility (CSR) Against Corporate Value with Price Earnings Ratio as Moderating Variables on The Main Sectors	212
The Determinant Factors of Indonesian Public Listed Companies' Debt Policy	227
The Influence of Internet Financial Reporting and Degree of Information Disclosure on Company's Website to the Frequency of Stock Trading on Trading, Services, and Investment Company Listed on Indonesian Stock Exchange	253
Combined Effect of Executive Stock Option Granting and Blockholder Ownership on Firm Performance in Malaysia.....	265
The Role and Influence of Corporate Leader Values on Corporate Governance Mechanisms and Financial Reporting Quality.....	276
The Relationship Between Leadership Behavior to Organizations Commitment, Budgetary Participation, and Job Satisfaction in Creating Good Government in Bengkulu City	319



Audit Fees: The Role of Auditor Type and Audit Market Competition	333
The Effect of Board Diversity, Multiple Directorships and Ownership Structure on Firm Performance.	356
The impact of Corporate Governance on Dividend Payment Policy: empirical evidence from Iranian Listed Companies.....	380
Establish a Balance Scorecard Approach to Enhance Zakat Distribution System in East Coast Region .	391
Corporate Governance and Firm Value: Evidence from Iranian Listed Companies	406
Financial literacy and communication of financial ratios	417
The Relationship between Intensity of Competition, Delegation of Authority, Management Accounting and Control Systems Changes, Organizational Performance (Empirical Study in Manufacturing Companies Listed in Indonesian Stock Exchange).....	440
Hubungan Di Antara Keadilan, Kepercayaan Dengan Pematuhan Cukai Individu Di Malaysia	451



Quality of Human Resources and Application of Income Tax Accounting at Construction Company in Palembang City

Bambang Bemby S, Endika Hady Pratama, Mukhtaruddin, Aryanto and Abukosim,
Economics Faculty, Sriwijaya University, Palembang, Indonesia

ABSTRACT

In preparing and presenting financial statements, the company has been using the power of accounting staff. The accounting staffs is required to have a deep understanding of the standards and provisions concerning the preparation of financial statements, one of which is on SFAS No.46. The application of income tax accounting depends on the quality of human resources in a company.

This study aims to determine the effect of human resources consisting of education, training, and work experience possessed HR itself particularly to the application of the accounting staff of accounting for income tax. The object of the research is the construction company listed on the Primary Tax Office Palembang Ilir Barat.

Sources of data in this study were obtained from the results of questionnaires to human resources to accounting Construction Company listed on the Primary Tax Office Palembang Ilir Barat encountered directly in the companies concerned. The results of this study have indicated that all the independent variables: education, training, and work experience either simultaneously or partial significantly affect the application of income tax accounting. To improve the application of income tax accounting in companies, especially in the construction company in the city of Palembang, the authors suggest that the company to be more selective in their recruitment including accounting staff.

Keywords: *Quality of Human Resources, Application of income tax accounting, Construction Company*

INTRODUCTION

Background

In Indonesia, the tax receipt is one of the greatest countries in each year. Tax is a very important source of revenue in terms of implementing and enhancing national development aimed at improving the welfare of the community. Below is a table of tax contribution to state revenues:

Table 1: Contributions against State Income Tax

Year	Tax Receiver		Non Tax Receiver		National Receiver
	Million(Rp)	Contribution(%)	Million(Rp)	Contribution(%)	Million(Rp)
2007	490.988	69,5	215.120	30,5	706.108
2008	658.701	67,3	320.604	32,7	979.305
2009	619.922	73,2	227.174	26,8	847.096
2010	723.307	72,9	268.942	27,1	992.249
2011	873.874	72,5	331.472	27,5	1.205.346
2012	1.016.237	74,9	341.143	25,1	1.357.380

Sources: Center Statistical Bureau 2013

Based on the above table, it can be explained that the contribution of tax revenue to state revenue are likely experiencing an increase every year. Seeing these conditions, the government must carefully and decisively to regulate and curb tax revenue by creating a device or rules to guide the implementation of the tax revenue that is acceptable to all stakeholders. One of interest parties is firm. The Company is a party that has the obligation to pay taxes to the government, among others, by paying income tax. Income



tax is a type of tax imposed in Indonesia. In general, the income tax is an additional tax imposed on the economic capability acquired or received by an individual or business entity both from Indonesia and outside Indonesia. To see the condition and performance of a company, then the company must prepare financial reports with the aim of presenting accurate information about the state of the economy the company for a certain period. The financial statements must be prepared and presented by Financial Accounting Standards. For many reasons, this standard may differ from the tax provisions also utilize accounting information. As an example of what often happens is the commercial profit and taxable income differ often caused by the difference between the recognition of income and expenses in accordance with GAAP and tax laws. Indication of the difference is that there is a difference of time (temporary differences) which resulted in differences in the recognition of current tax expense to the recognition of tax payable. In response, the Indonesian Institute of Accountants imposes SFAS 46, Accounting for Income Taxes that have experienced the last revision in 2013. SFAS 46 requires companies to account for the tax consequences in the current period and future periods to calculate and recognize the deferred tax over the future effects of tax using the balance sheet liability method or asset/ liability method. To be able to calculate and recognize the deferred tax is based on balance sheet liability method set forth in SFAS 46, the main thing to understand is the concept of temporary timing differences-temporary differences. Timing differences are differences in accounting and taxation that are temporary, which means the overall revenue or expense accounting or tax is actually the same, but just different allocations each year. Although it has become effective since a few years ago, but there are still many obstacles in its application for the company. The problem is due to lack of socializing and training to the taxpayer about the knowledge of the application of SFAS 46, particularly in the calculation of how much deferred tax should be recognized by the company.

The taxpayer is preparing and presenting financial statements have been using of human resource accounting (Accounting Staff). Human resource accounting is an office that is responsible for the financial activities of a written report. In addition, this position is required to understand the tax issues that apply in Indonesia. Chaer (2002) stated that the collapse of the economy in Indonesia as a result of social and political upheavals, economic and culture, and is significant HR issues. In the history of human beings as subjects noted that the role of human resources to address the crisis that swept across the nation of Indonesia. HR is the backbone of operations that must continue to improve the quality, both internally and externally. This is in line expressed by Karnoto (2004), human resources professional, good morals, honesty, and integrity are the backbone of the company. The role of accounting staffs is very important in preparing the financial statements.

HR itself can be assessed based on education, training, and work experience of HR itself. Education is one of the factors on the quality of human resource assessment. Education itself can reflect a person's level of thinking in the work. Of education, someone will get the sciences that would be very useful in the future. In addition, to increase the knowledge gained from education, one must follow the training in accordance with the field work. However, two things are not enough to assess whether the quality of HR can be said or not. HR needs a lot of work experience would work the same. The more experience a person's work, the less likely that someone made a mistake in his work. In other words, human resource accounting must have a deep understanding of the standards and provisions of the financial statements. SFAS 46 is one of the standards that must be understood by the human resource accounting. SFAS 46 is about the income tax accounting. Companies need to provide training SFAS 46, Accounting for Income Taxes to the accounting staff, given the complex application and required a deep understanding. Proper application of SFAS 46 will give you the information generated financial statements more relevant and informative for the tax consequences in future due to temporary differences that occurred in the past are now becoming apparent in the financial statements.

Problems that occur at this time that the company needs help from external parties is a tax consultant in presenting the financial statements of the company, whereas the task of doing just tax consultants and tax issues to deal with a company not on the financial statements. This could be due to the low quality of



human resources in the company's accounting thus causing errors in the presentation of financial statements, particularly in applying the tax accounting. Based on the results of previous interviews were conducted by researchers of the 30 companies of the object in this study that as many as 28 companies (Construction Company listed on the Primary Tax Office Palembang Ilir Barat use of external assistance (tax consultant) to resolve the problems, especially financial statement presentation in the application of tax accounting. When viewed from the HR function itself, should HR in accounting must have the ability, knowledge, as well as a good understanding of accounting as a whole, especially regarding the accounting for income tax contained in IAS 46. The interview results also concluded that most of the construction companies that are the object of research is not applying the income tax accounting in accordance with the provisions of SFAS 46, there were 137 companies that have not implemented properly accounting for income tax. Doing so may result in the company's financial statements is irrelevant, uninformative, and not in accordance with the provisions of applicable accounting standards. In addition, it can cause the amount of tax debt owed by the company to be larger (smaller) than that should be paid by the company keeping in mind that there is a burden (income) that according to SFAS 46 are not shown in the financial statements so that such companies get warning even fined by the tax authorities for the amount of tax payable is not paid in accordance with proper.

Based on the observations that have been made, the main factors that cause why the income tax accounting is not (yet) implemented is HR accounting department of the company. Based on results of questionnaires that have been done, some of the companies have accounting staff of high school graduates and diploma 3, so it is likely that the knowledge they get is not enough to do the job. In addition, few of the accounting staff at the research object ever does training on SFAS 46. This indicates that human resource accounting has an important role in the application of income tax accounting. Selection of construction companies listed on Primary Tax Office Palembang Ilir Barat as the research object because construction companies make a major contribution to tax revenues than other sectors. It can be seen from the following table:

Tabel 2. Tax Receiver in Primary Tax Office Palembang Ilir Barat

Year	NET RECEIVERT	PAX PAYER CONTRIBUTION	CONTRIBUTION
2012	Rp 588.080.992.044,00	Rp 375.213.412.302,00	64%
2011	Rp 429.760.202.245,00	Rp 259.052.673.372,00	60%
2010	Rp 405.060.590.646,00	Rp 223.237.758.170,00	55%
2009	Rp 271.742.917.792,00	Rp 147.904.321.450,00	54%
2008	Rp 230.804.501.600,00	Rp 103.790.564.137,00	45%

Sources: Tax Offices KPP Pratama Palembang Ilir Barat 2013

This study was conducted to follow up on the basis of suggestions from some previous research on the application of SFAS 46 were not maximized due to low quality of human resources owned accounting firm. One goal of this study was to evaluate the performance of human resources, especially in the field of accounting. According Darwanis and Desi (2009), by evaluating the competence and quality of a person, the company will be able to predict the performance of the person. In addition, this study replicates the research of Winidyaningrum and Rahmawati (2010). The fundamental difference between previous studies with this study is previous research using human resources factors and use of information technology as an independent variable and the reliability and timeliness of financial reporting in local government local government as the dependent variable. While this study uses a factor of education, training and work experience of human resource accounting as independent variables and the application of income tax accounting.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Learning Curve Theory

Learning Curve Theory expressed by Shu Liao S stating that an employee has the education and experience levels are high for a job, then the time will be needed to complete the job getting short so that is also expected to increase its performance (Siswanto, 2012). Psychological theory Stimulus-response relationship (SR) always assume that the long experience to solve new problems. That is, if one ever made a mistake, and the mistake has been corrected, the same mistakes will not be done again (Chaer, 2003). The theory of learning by Faculty-psychology (Life Science Resources), according to the theory of the human soul consists of various powers like the power of thinking, knowing, remembering, and others watched. These forces can develop and function when trained with the materials and specific ways (Ahmadi, 2002). Thus, education, experience and training are factors that can increase a person to live a quality of life to a more positive direction or can help a person to do the job.

Accounting for Income Taxes

The accounting treatment of the income tax is set by SFAS 46 of presentation income tax on the financial statements and the disclosure of information that is relevant. Changes in the approach used by the Financial Accounting Standards especially for income tax accounting of deferred income statement approach or method being a balance sheet approach or Asset-Liability Method undeniable has added to the complexity of the calculation of income tax due to the recognition of deferred tax on the balance sheet. SFAS 46 is to prescribe the accounting treatment for income taxes. The main problem in accounting for income taxes is how to account for the tax consequences in the current period and future periods for the following matters (SFAS 46, paragraph 2): (a) Recovery of the carrying amount of the asset or settlement of the carrying amount of liabilities, giving rise to acknowledge the consequences of deferred tax assets or liabilities, with a few exceptions. (b) Transactions or other events in the current period that are recognized in the income statement with the consequences should be charged or credited directly to equity, and (c) Adjusting confession deferred tax assets from the rest of the loss is compensated for the following year, presentation income tax on the financial statements and the disclosure of information relating to income tax. The scope of SFAS 46 is as follows: (a) Includes final income tax treatment, which means that the tax liability that has been completed and the income subject to income tax cannot be combined with other income taxable income that is not final. In accordance with tax legislation, income subject to final income tax no longer is reported as taxable income, the entire burden in respect of income subject to final income tax may not be deducted. Therefore, no temporary difference not recognized the existence of assets or deferred tax liabilities, (b) Include cancellation of paragraph 77, SFAS 16 which states if the company chooses to calculate the tax according to the accounting profit, the difference in the calculation of the tax payable is calculated (as calculated according to taxable income) due to differences in timing of the recognition of income and expenses for accounting purposes by tax purposes accommodated in the deferred income tax estimates, grouped some of the other assets and allocated to load taxable income for years to come.

SFAS 46 relating to Income Tax reporting there are some important terms you need to know, following the basic understanding of these terms: (1) Deferred tax is the amount of income tax expense or income taxes payable for future periods as a result of temporary differences and residual compensation for losses, (2) Current Tax is the amount of income tax payable on taxable income for the period, (3) Tax Expense or Income Tax is the aggregate amount of current tax and deferred tax are taken into account in the calculation of profit and loss in the period, (4) Deferred Tax Liability is the amount of income tax payable for future periods as a result of taxable temporary differences, (5) Deferred Tax Assets is the amount of income taxes recoverable in future periods as a result of deductible temporary differences and residual compensation for losses, and (6) Temporary differences are differences between the carrying amounts of



assets or liabilities and their tax bases (the DPP). Temporary differences may be either: (a) Deductible temporary differences are temporary differences that give rise to an amount that may be deducted in computing taxable income in future periods when the carrying amount of the asset is realized or the liability is settled carrying value, and (b) Taxable temporary differences are temporary differences that give rise to a taxable amount in the computation of taxable profit in future periods when the carrying amount of the asset is realized or the liability is settled carrying value. Deductible temporary differences will result in deferred tax assets, due to the economic benefits that will be earned taxpayer in the form of a deduction from the taxable income in the future. While the taxable temporary differences give rise to deferred tax liabilities will be in the current period timing differences or temporary differences, because there are income tax liability in future periods.

Recognition of Current Tax Assets and Liabilities Current Tax

Total current tax for the current period and prior periods is recognized as a liability has not been paid. If the amount already paid for the current period and prior periods exceeds the amount of tax payable for such periods, the difference is recognized as an asset. Benefits relating to tax losses that can be pulled back to recover current tax of a previous period shall be recognized as an asset. If the tax loss is used to recover current tax of prior periods, the entity recognizes the benefit as an asset in the period in which the tax loss occurs because there may be benefits received entity and these benefits can be measured reliably.

Recognition of Deferred Tax Assets and Deferred Tax Liabilities

Deferred tax assets are the amount of income taxes recoverable in future periods as a result of deductible temporary differences and residual compensation for losses. Deferred tax assets are recognized for all deductible temporary differences to the extent that could potentially be used to reduce taxable income in the future, except those arising from: (1) Negative goodwill recognized as deferred income from the business combination, (2) the initial confession of assets and liabilities in a transaction that is not a business combination transaction and has no effect on the commercial income and taxable income. The deferred tax liability is the amount of income tax payable for future periods as a result of taxable temporary differences, except that arising from: (1) Goodwill amortization is not deductible for tax purposes, and (2) Initial recognition of an asset or liability in a transaction that is not a business combination transaction and has no effect on the commercial income and taxable income.

Recognition of tax losses that can be compensated

The balance of unused tax losses are recognized as deferred tax assets when it is probable that future taxable profit will be available against which it comes. But keep in mind, if the taxable income may not be available in sufficient quantity to be compensated with tax losses can be utilized, the deferred tax assets are not recognized.

Recognition of Current Tax and Deferred Tax

Current tax and deferred tax is recognized as income or expense in profit or loss for the period, except for income tax derived from: (a) Transactions or events that are directly credited or charged to equity in the same period or different periods, or (b) Business combination that is in substance the acquisition. Current tax and deferred tax shall be charged or credited directly to equity if the tax relates to transactions that are credited or charged directly to equity.

According to estimates Presentation of SFAS 46; (a) Tax Assets and Liabilities. Tax assets and liabilities should be presented separately from other assets and liabilities in the balance sheet. Deferred tax assets and deferred tax liabilities should be distinguished from current tax assets and current tax liabilities. If the financial statements, current assets and liabilities are presented separately from non-current assets and liabilities of the asset (liability) Deferred tax should not be presented as an asset (liability) smoothly, (b) Eliminating each other (offset). SFAS 46 does not state explicitly the deferred tax asset may or must be compensated (offset) of deferred tax liabilities in the balance sheet presentation. SFAS 46 states that the current tax assets should be compensated (offset) with current tax liabilities and the net amount presented in the balance sheet should be; (c) Tax Burden. Expense (income) taxes related to profit or loss from



ordinary activities should be presented separately in the income statement; (d) Final Income Tax. If the carrying amount of an asset or liability related to final income tax differs from the Taxable Income Basis, the difference is not recognized as deferred tax assets or liabilities. On income subject to final tax, income tax expense is recognized in proportion to the revenue recognized in the current period. The difference between the final tax payable and the amount charged as expenses in the calculation of current tax income is recognized as Final Income Tax Income Tax Prepaid and Accrued Final. Estimated prepaid final tax was shown separately from final tax accrued.

Disclosures in SFAS 46

The following matters shall be disclosed: (a) The main elements of expense (income) tax, (b) The amount of current tax and deferred tax transactions which are charged or credited to equity, (c) Expense (income) tax from extraordinary items recognized in the current period, (d) A description of the relationship between tax expense (income) tax and accounting profit in either or both of the following forms: (i) a reconciliation between tax expense (income) and the theoretical tax accounting profit and tax rates applicable, by revealing the basis for calculating the applicable tax rate ; or (ii) a reconciliation between the effective tax rate on average (average effective tax rate) and the applicable tax rates, by revealing the basis for calculating the applicable tax rate, (e) A description of the changes in applicable tax rates and comparison with the tax rates applicable in the previous accounting period, (f) The number (and limit the use of time, if any) deductible temporary differences and the remaining loss carry forward to next year, which is not recognized as deferred tax assets on the balance sheet, (g) For each group of temporary differences and losses for each group can be compensated to the following: (i) the amount of deferred tax assets and liabilities are recognized on the balance sheet presentation for each period; (ii) the amount of tax expense (income) tax deferred, (h) recognized in the income statement if the number is not visible from the change in the amount of deferred tax assets or liabilities are recognized on the balance sheet, and (i) To continue operating, the tax burden is attributable to: (i) the gain or loss on discontinued operations; and (ii) the profit or loss from ordinary activities was discontinued operations for the reporting period, together with a number of previous accounting periods presented in the financial statements.

Deferred Income Tax Calculation

Deferred income tax can be calculated by multiplying the time difference is going on with the tax rate in effect at the time the asset is realized or the liability is settled. Typically, the rate used is the highest income tax rate is 30%, although the actual rate is progressive. If the current year tax loss occurs, the deferred income tax can be calculated in the same way, i.e. the average effective rate, if the assumption is 30%, then 30% multiplied by the losses that occurred.

Quality of Human Resources are explained by (a) Education. Qualified human resources cannot be separated from the educational factor. Education is an important thing that was greatly affecting a person's development. Basically the definition of education (Education Law No.20/3003) is a conscious and deliberate effort to realize the learning process so that learners are actively developing the potential for him to have the spiritual strength of religious, self-control, personality, intelligence, noble character, and the skills needed themselves and society. Education is believed to instill knowledge, skills, and values so that one can improve his ability. This is consistent with that expressed by Ghazali (2000) that education has a significant influence on a person's learning capacity and productivity. Through education, the quality of a person can be improved in many aspects. People who are educated will be more creative and open to renewal, will be more dynamic in thinking, to foster self-confidence and can adapt to the social environment. If education has been obtained, then the cognitive abilities will increase and it will automatically increase the productive capacity of the workforce. Educated people will be more rational in thinking and acting as well as understand the duties and responsibilities given well. Saputra (2002) stated that education is a catalyst in the development of human resources. Education is one factor which can indicate the quality of human resources. Qualified human resources have a competitive advantage and it can only be acquired through education, both formal and informal education (Winidyaningrum and Rahmawati, 2010). Formal education can be done by giving knowledge of theory, analytical skills, and



the development of logic. While informal education can be done by providing knowledge about religion, ethics, manners, and socialization to the environment. The higher education is taken, the higher the owned intellectual. Employees who are more educated/more educated will participate in making decisions (Warisno, 2009). Accounting staff that has relevant education to the job will have the ability, as reflected in his work (Saputra, 2002), (b) Training. In addition to education, an important factor in determining the quality of one's work is to follow a lot of training. According Huliah et al (2012), training is an activity that aims to improve and develop the attitudes, behavior skills, and knowledge of its employees in accordance with the wishes of the company. Training will provide benefits to productivity, morale, cost reduction, stability and flexibility to organizations facing environmental uncertainty. The main purpose of training can be divided into five areas, namely: (1) To improve the skills of employees in accordance with the changes in technology, (2) To reduce the time to learn a new employee to become competent, (3) To assist operational issues, (4) To prepare the employees in the promotion, (5) To give an employee orientation to learn more about the organization. Training is important for employees, both new employees and employees of the old. This is in line with the statement Saputra (2002) which states that the quality of human resources can be achieved through education and training regularly programmed and integrated by relevant institutions authorized. The main purpose of training is to improve and eliminate problems associated with employee performance. The training is intended to get workers who have the knowledge, skills, abilities, as well as a good attitude to perform a specific job (Lopez, 2008). Training is an important factor in improving of human qualities to determine the success of achieving corporate goals. Moekijat (1991) says that the training required helping employees increase the skills and knowledge that are closely related to the employee's job. Lubis (2008) adds that there are three conditions that must be met in order for an activity can be called the training, namely: a) Training should help employees more functionality; b) Training should lead to a change in habits, information, and knowledge that the employee apply in their work; and 3) Training must relate to a specific job or jobs that are being implemented which will be given in the future. Based on the these statements, it can be concluded that training is an activity to improve the ability of the person in relation to the accounting activity that can assist the employee in performing his job in order to improve the knowledge, skills, and attitudes of the employees. Therefore, training should be conducted in accordance with the real needs of the company, (c) Work Experience. The ability of a person is not only measured by education and training only, but work experience contributed greatly to a person's ability to handle his job, especially for a complicated job and requires special expertise. Is the length of a person's work experience in performing the same tasks and work according to his ability? In other words, work experience is a onetime used to acquire the knowledge, skills, and attitudes appropriate to the task and job. Experience can be gained through experience or practice directly or indirectly could also, as of reading. Warisno (2009) states that a firm will tend to choose an experienced workforce of the inexperienced. This is because a more experienced workforce qualified to carry out the work and responsibility given company can be done in accordance with the provisions of the company. Employee performance is influenced by the work experience of the employee, the longer the employee experience will be easier to resolve product and the less experienced employees will affect the ability to produce employee in completing a product (Saleh et al, 2013). Besides past performance on similar work can be the best indicator of performance in the future. In the experience of human resource accounting department, will be very helpful in the process of presenting quality accounting information. The more extensive a person's work experience, the more skilled do the job and more perfect patterns of thinking and attitudes in the act in order to achieve the stated goals (Arfan and Edi, 2009).

Hypothesis Development

Effect of Human Resources Education on Application Income Taxes Accounting

Theoretically, education is learning to prepare individuals for different jobs in the future. Education is designed to allow workers to learn about the different jobs within the same organization. According Warisno (2009), the higher education one achieves the higher the level of understanding and knowledge



gained to apply their job. The first hypothesis is Education HR has a significant influence on the application of income tax accounting

Effect of Human Resources Training on Application Income Taxes Accounting

Training is a learning process that involves the acquisition of skills, concepts, rules, or attitudes to improve workforce performance (Huliah et al, 2009). According to the first paragraph of Article 9 of Law 13 of 2003, is the overall job training activities to provide, acquire, improve, and develop job competence, productivity, discipline, attitude, and work ethic at a certain level of skill and expertise and qualifications in accordance with the level of office and work. The aim of the training program is to increase the performance of individuals in certain positions or functions. According Saputra (2002) training was greatly affects a person's performance level, a growing number of workers doing the training will increase the performance of the workers. Based on the above, the second hypothesis training has a significant influence on the application of income tax accounting

Effect of Human Resources Work Experience on Application Income Taxes Accounting

Work experience someone shows the types of work ever done one and presents a great opportunity for someone to do a better job. The more extensive a person's work experience, the more skilled do the job and more perfect patterns of thinking and attitudes in acting to achieve its intended purpose (Huliah et al, 2012). Based on the above, the third hypothesis is HR Work experience has a significant impact on the application of income tax accounting.

Theoretical Framework

Based on the analysis of the theoretical basis, previous research, and the research hypothesis, it can be described a theoretical framework as follows:

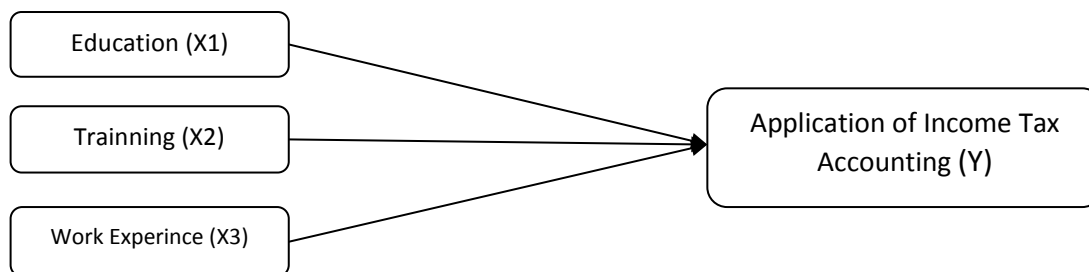


Figure 1. Theoretical Framework

III. RESEARCH METHODOLOGY

Population and Sample

The population used in this study is all listed construction companies in the Primary Tax Office Palembang Ilir Barat with the number reached 288 companies. Selected sample of the population is considered representative of the population. The sample in this study is using purposive sampling method, with the goal of providing equal opportunity for each company to be selected as sample (Sumarni and Wahyu, 2005:76). The criteria used in determining the sample is as follows (1) The company does not disclose taxes receivable and taxes payable on the financial statements (balance sheet), and (2) The Company does not use the services of a tax consultant. Based on the sampling technique to be done, it will get some samples to be used for processing in this study.

Table 3 Sample Research

Sample Criteria	Number of Company
Construction Company listed in Primary Tax Office Palembang Ilir Barat	288
Company has not presented of tax payable in financial statement	(137)
Company has used of Tax Consultant Services	(72)
Total Number of Company Sample.	79



Types and Sources of Data

Conducted a survey method is collecting data using questionnaires. Questionnaire is a written list of questions that have been previously formulated which will be answered by the respondents. In producing research data, questionnaires conducted by researchers by distributing questionnaires directly to human resources accounting in construction companies registered in Primary Tax Offices Palembang Ilir Barat. In this study, researchers took the study a variable instrument that have been developed and tested its validity by previous researchers. In making the questionnaire, the researcher deliberately enter negative statements in some instrument variables. It aims to avoid bias and provide control of the research results due to respondents who sometimes less earnest in filling out the questionnaire.

Operational Definition and Measurement of Variables

The dependent variable in this research is the application of Accounting for Income Taxes. Measurement of these variables using a questionnaire adapted from a questionnaire study Huliah et al (2012) with any changes as needed. Indicators in this study were (1) Knowledge and understanding of SFAS 46, (2) application of income tax accounting in accordance with the provisions of SFAS 46, (3) Presentation of Financial Statements are reasonable, (4) Disclosure of transactions balances related to tax accounting income, (5) Disclosure of accounting changes. This study used a questionnaire instrument response measurement scale of 5 (five) points Likert scale. The following answer choices along with the code and the answer to the fifth score of the questionnaire code:

Table 4 Codes And Score Questionnaire Answers

Code	Alternative Answer	Score
SS	Strongly Agree	5
S	Agree	4
KS	Less Agree	3
TS	Disagree	2
STS	Strongly Disagree	1

Education (X1)

Education is an important factor which greatly affects a person's development. The higher education pursued the higher the owned intellectual experience. Adequate formal education with a background in accounting for human resource accounting human resource will facilitate in carrying out routine work. Human resource accounting education relevant to the job will have the ability, as reflected in his work. Measurement of these variables using a questionnaire adapted from the questionnaire research Saleh (2013). Educational factors measured by indicators such as: (1) The level of formal education, (2) Competence/capability in the field of education. This study used a questionnaire instrument response measurement scale of 5 (five) points Likert scale. Choice answers along with the code and the answer to the fifth score of the questionnaire code is the same as the previous variable.

Training (X2)

In addition to education, an important factor in determining the quality of one's work is to follow a lot of training. According to experts, the training is an activity that aims to improve and develop the attitudes, behavior skills, and knowledge of its employees in accordance with the wishes of the company. Measurement of these variables using a questionnaire adapted from a questionnaire study Huliah et al (2012). Indicators in the measurement of training factors are as follows (1) The period of training, (2) training materials, (3) Continuity of training. This study used a questionnaire instrument response measurement scale of 5 points Likert scale. Choice answers along with the code and the answer to the fifth score of the questionnaire code is the same as the previous variable.

Work Experience (X3)

Experience can be gained through experience or practice directly or indirectly could also, as of reading. Besides past performance on similar work can be the best indicator of performance in the future. In the experience of human resource accounting department, will be very helpful in the process of preparing accounting information quality. Measurement of these variables using a questionnaire adapted from a questionnaire study Huliah et al (2012). Indicators in measuring work experience among other factors: 1) The period of work in the field of accounting, 2) Work experience in the field of accounting. This study used a questionnaire instrument response measurement scale of 5 (five) points Likert scale. Choice answers along with the code and the answer to the fifth score of the questionnaire code is the same as the previous variable.

Data Analysis Techniques

Analysis of Response Rate

The response rate is the proportion of the sample that completed the questionnaire. The number of questionnaires sent, who made it back, until the number of questionnaires that can be used as an instrument to be processed should be recorded and categorized, then calculated the proportion in its entirety.

Test Validity

One of the measuring instruments can be said to be valid if the answer carefully about the validity of the measure. A questionnaire as valid, if the questions on the questionnaire was able to reveal something that will be measured by the questionnaire. Testing the validity of using the Pearson correlation, i.e. by calculating the correlation between the scores of each of the questions with a total score has a significant level below 0.05, then the item is declared valid question, and vice versa (Ghozali, 2006).

Test Reliability

Instruments said to be reliable if there are similarities data in different times. A questionnaire said reliable / reliable, if the answer to question one is consistent / stable over time. Reliability test is used to measure the variables used that are completely free of errors, thus producing consistent results, although tested many times. If the Cronbach alpha above 0.6, data has a high reliability (Ghozali, 2006).

Multiple Regression Analysis

The analysis technique used in this research is the technique of multiple linear regression analysis to obtain a comprehensive picture of the relationship between one variable with another variable. This study were using a factor of education, training and work experience of human resource accounting as independent variables and the application of income tax accounting in preparing the financial statements as the dependent variable. To find out if there is a significant effect of independent variables on the dependent variable we used linear regression models multiple (multiple linear regression method) that replicates the research of Winidyaningrum and Rahmawati (2010) is formulated as follows:

$$AITA = \alpha + \beta_1 \text{EDU} + \beta_2 \text{TRAIN} + \beta_3 \text{WE} + e$$

Test coefficient of determination (R²)

The coefficient of determination (R²) was essentially measures how far the model's ability to explain variation in the dependent variable (Ghozali, 2006). This test is done by looking at the value of the coefficient of determination R² which is a non-negative scale. The value of the coefficient of determination was between zeros to 1. If R² = 0 or close to 0, then the relationship between the two variables is very weak or no relationship at all. When R² = +1, or close to 1 then the correlation between the two variables is said positive and very strong.

Research Object Description

Objects in this study are listed construction companies in the Primary Tax Office Primary Palembang Ilir Barat. The construction companies will be selected through the method of selecting the sample is by using purposive sampling method based on the criteria that have been determined by researchers to produce research object that has met the criteria designed by the investigators. Based on the sampling method that has been done, then the number of objects that will be tested in the



company of this research is to address as many as 79 companies spread over the area listed in Primary Tax Office Palembang Ilir Barat.

Demographic Data Object Description Research

HR accounting in each company has different ages. For the age group between 20-30 are 55%, equivalent to 43 companies that have HR accounting between the ages of 20-30 years. For the age group between 31-40 are 25%, equivalent to 20 companies that have HR accounting between the ages of 31-40 years. For the age group between 41-50 are 11% or the equivalent of nine companies that have HR accounting between the ages of 41-50 years. As for the age category > 50 only contained 9%, equivalent to 7 HR accounting firm that has more than 50 years old. Of the 79 companies that are the object of research, there are only 11% or the equivalent of 9 companies that fill the position as manager of the accounting department in a questionnaire study. As for the position as accounting staff are 89%, equivalent to 70 companies. Accounting staff at the construction company has a research sampled a variety of educational levels. For the high school level has a number of 11 people, equivalent to 14% of the total study sample. On the other hand, to the level of Diploma has the number 15 or 19% of the total study sample. As for the level of Bachelor degree has a number of 53 people, equivalent to 67% of the total study sample. From these data it can be concluded that there were 11 companies have accounting staff who graduated from high school, 15 companies have accounting staff from D3, and 53 companies have accounting staff graduated from Bachelor degree.

There are 19 companies where the accounting staff at the company has never done either training or training on SFAS 46 accounting training in other fields. In addition there are 27 companies in which the company's accounting staff had done training in accounting but have not done the training on SFAS 46 (Accounting for income tax). Thus, there are only 33 companies out of 79 companies that are the object of research in which the accounting staff of the company who had conducted training on SFAS 46. Each accounting staff has diverse work experience. There are 17 companies where accounting staff have work experience in accounting more than 10 years. A total of six companies in which the company's accounting staff has work experience in accounting between 8-10 years. A total of 12 companies in which the company's accounting staff has work experience in accounting between 8 to 7.9 years. A total of 21 companies in which the company's accounting staff has work experience in accounting between 2 - in 4.9 years. As for the accounting staff that have experience working in the field of accounting for less than 2 years as many as 23 companies.

Description of Research Variables

Application of Accounting for Income Taxes

The application of income tax accounting is measured using indicators that have been described in the previous chapter, namely 1) Knowledge and understanding of SFAS 46, 2) application of income tax accounting in accordance with the provisions of SFAS 46, 3) Presentation of Financial Statements fairly, 4) Disclosure of transactions balances related to income tax accounting, 5) Disclosure of accounting changes.

III. ANALYSIS AND DISCUSSION

Results Analysis of Response Rate

The research object in this case is a construction company which is listed on the Primary Tax Office Palembang Ilir Barat. The numbers of construction companies listed on Primary Tax Palembang Ilir Barat are totaling 288 companies for 2013. From all listed construction companies will do the selection of the research sample are using purposive sampling method. Of the election can be generated that amount of construction company research sample amounted to 79 companies. In this study the distribution of questionnaires to the return of the questionnaire requires a period of approximately one month. Questionnaires were distributed to Construction Company accounting staff made the object of research.

Table 5 Response Rate of Questionnaire



Items	Number	Percentage
The number of questionnaires distributed	79	100%
The number of questionnaires were not returned	0	0
The number of questionnaires can be used	79	100%

Descriptive Statistics Analysis

Based on the descriptive statistical analysis of the data, the data obtained as much as 79 data for each variable with the number of objects of research as much as 79 construction companies. Descriptive statistical analysis of the results will give an overview of the data by looking at the average value (mean), standard deviation, variance, maximum value and minimum value.

The education variables indicate that for all the questions have answers level with the minimum and maximum values are equal, respectively 3 and 5. For the average value (mean) of all questions is 4.22, respectively; 4.23; 4.44; 4.47; and 4.18. It shows that the average number of responses to questionnaires to all questions on the education variable is the value of 4 (Agree).

variabel pelatihan menghasilkan bahwa semua pertanyaan memiliki tingkat jawaban dengan nilai minimum dan nilai maksimum yang sama masing-masing 3 dan 5. Untuk nilai rata-rata (*mean*) semua pertanyaan adalah masing-masing 4,28; 4,15; 4,25; 4,39; 4,22; dan 4,41. Ini menunjukkan bahwa yang menunjukkan bahwa rata-rata jumlah jawaban kuesioner untuk semua pertanyaan pada variabel pelatihan adalah nilai 4 (Setuju).

The variable work experience suggests that all the questions have answers level with the minimum and maximum values are equal, respectively 3 and 5. For the average value (mean) of all questions is 4.28, respectively; 4.24; and 4.29. It shows that that shows that the average number of responses to questionnaires to all questions on work experience variable is the value of 4 (Agree).

The dependent variable is the application income tax accounting (SFAS No.46) indicates that all questions have answers level with the minimum and maximum values are equal, respectively 3 and 5. For the average value (mean) of all questions is the 4.18 respectively; 4.14; 4.22; 4.10; 4.16; and 4.14. It shows that the average number of responses to questionnaires to all questions on the application income tax accounting variable is the value of 4 (Agree).

Multiple Regression Analysis

Testing the hypothesis is using of multiple regressions. Multiple regression analysis technique is used to obtain a comprehensive picture of the relationship between one variable to another variable. It can be composed of multiple linear regression equations as follows:

$$\text{AITA} = 6,186 + 0,379\text{Edu} + 0,294\text{Train} + 0,324\text{Exper}$$

Based on the above equation can be explained that their relationship between the three independent variables: education, training, and work experience is positive on the dependent variable is the application of income tax accounting, meaning that the application of income tax accounting has been linked linearly with education, training, and work experience. This shows that the application of income tax accounting depends on the education, training, and work experience of human resources. While the above is a linear relationship can be described by algebraic sign of each regression coefficient is: If the level of education increased by one unit then this will affect to the application of income tax accounting increased by 0,379 units and other variables held constant. Similarly for the second variable if the level of training that is increased by one unit then this will affect the application of income tax accounting increased by 0.294 units and other variables held constant. Finally for the third variable, If work experience increases one unit will be followed by increased application of income tax accounting for 0,324 units and other variables held constant. Can be described by an equation that estimates the change or variance application of income tax accounting is highly dependent on the change or variance of three independent variables in the model equations. So it can be said the three-way relationship of independent variables on the dependent variable is positive.

Simultaneous Effect Test



The test is to determine whether the independent variables simultaneously affect the dependent variable. If the probability level of less than 0.05, it can be said that all the independent variables jointly affect the dependent variable. The following table is used to investigate the effect of the quality of human resources consist of education, training, and work experience simultaneously to the application of income tax accounting.

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	83,431	3	27,810	23,166	,000 ^a
	Residual	90,037	75	1,200		
	Total	173,468	78			

a. Predictors: (Constant), Experience, Education and Training

b. Dependent Variable: App of SFAS 46

Based on the above table the results obtained for the calculated F 23.166 with a significance level of 0.000. Since the level of significance <0.05 and $F_{count} > F_{table}$ (2.727), it can be concluded that education, training, and work experience together significant effect on the application of income tax accounting. This suggests that the application of income tax accounting depends on the level of education, training, and work experience were possessed by human resources, especially the accounting staff.

Individual Parameter Significance test

In this test will be known whether the independent variables: education, training, and work experience may partially affect the application of accounting for income tax as the dependent variable. Below is a table of that test has been done.

Model		Unstandardized Coefficients		Standardized Coefficients		t	Sig.
		B	Std. Error	Beta			
1	(Constant)	6,186	2,640			2,343	,022
	pendidikan	,379	,138	,280		2,740	,008
	pelatihan	,294	,100	,337		2,940	,004
	pengalaman	,324	,160	,212		2,019	,047

a. Dependent Variable: psak46

Based on the above table can concluded that (1) Influence of education on the application of income tax accounting has a t value of 2.740 is greater than t table value is 1.991 ($t_{count} > t_{table}$) and has a significance value of 0.008 is smaller than 0.05. Thus H1 is accepted that education has significantly influence the application of income tax accounting, (2) . Effects of training on the application of income tax accounting has a t value of 2.940 is greater than t table value is 1.991 ($t_{count} > t_{table}$) and has a significance value of 0.004 is smaller than 0.05. Thus H2 is accepted that training has significantly influence the application of income tax accounting, and (3) Effects of work experience on the application of income tax accounting has a t value of 2.019 is greater than the value of t table is 1.991 ($t_{count} > t_{table}$) and has a significance value of 0.047 is smaller than 0.05. Thus H3 is accepted that a significant effect of work experience on the application of income tax accounting.

Test coefficient of determination

Coefficient of Determination Test is used to determine the level of certainty of the nicest in the regression analysis revealed a compound with the coefficient of determination. This coefficient indicates how much percentage of variation of independent variables used in the regression model is able to explain the variation in the dependent variable. $R^2 = 1$ means perfect effect of independent variables on the dependent variable, otherwise if $R^2 = 0$ means that the independent variable has no effect on the dependent variable. Coefficients determination test results can be seen in the following table.

Table 8 Results Test coefficient of determination



Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	,694 ^a	0,481	0,46	1,096

a. Predictors: (Constant), pengalaman, pendidikan, pelatihan

Based on the results obtained in the above table shows that the results of the adjusted coefficient of determination (R²) of 0.460. This suggests that the major effect of independent variables: education, training, and work experience of the application of income tax accounting can be explained by the model equations for the remaining 46.0% and 54.0% influenced by factors outside the study.

Discussion of Results

Relationship education on Implementation of Accounting for Income Taxes

The first hypothesis (H1) says that there is a significant positive relationship between education factor to the application of income tax accounting. The results showed that the influence of education on the application of income tax accounting has a t value of 2.740 is greater than t table value is 1.991 (t count > t table) and has a significance value of 0.008 is smaller than 0.05. Thus H1 is accepted that education significantly influence the application of income tax accounting. In addition, the results also showed that the β value of 0.379, which means there is positive between educational factors of the application of income tax accounting which can be demonstrated by the increase in the level of the variable application of variable accounting for income tax will rise 0,379 assuming a fixed value of other variables. This supports the statement of Warisno (2009), the higher education one achieves the higher the level of understanding and knowledge gained to apply their job. The results of this study also have the same result with Winidyaningrum and Rahmawati (2010) which states that the education of human resources significant positive effect on the reliability of financial reporting area. The results are consistent with the Learning Curve Theory, which states that an employee has a level of education and experience that high for a job, then the time will be needed to complete the work more concise so that is expected to improve its performance.

Based on the explanation in the previous chapter that the study sample of 79, there are 11 companies that have accounting staff from the high school education. This indicates that the company's accounting staff on low quality and will have a negative impact on long-term company performance, especially in the field of accounting if it is not taken into account. These problems can be solved by means of the company should provide regular training on the science of accounting for income tax accounting, especially for the quality of the accounting staff (HR) can be increased. This is in line with the statement Saputra (2002) which states that the accounting staff who have relevant education will have the ability to work as reflected in his work. The statement is also supported by the opinion of dri Ghozali (2000) which states that education has a significant influence on a person's learning capacity and productivity.

From some of the above it can be concluded that the higher level of education of human resources, the higher the income tax accounting will be applied in the company. The company is expected to be selective in their recruitment, especially in the field of accounting for all the work to be done can be completed accurately, quickly, and in accordance with applicable standards. Employee performance is highly dependent on the level of education, the higher a person's education level, the higher the performance of the individual in question and will be useful in improving the quality of the person.

Relationship human resources training on the application of HR Accounting for Income Taxes

In the previous chapter it was mentioned that the second hypothesis (H2) is considered to have a significant positive relationship between the factors of training on the application of income tax accounting. The results showed that the effect of training on the application of income tax accounting has a t value of 2.940 is greater than the value of t table is 1.991 (t count > t table) and has a significance value of 0.004 is smaller than 0.05. Thus H2 is accepted that training significantly influence the



application of income tax accounting. In addition, the results also showed that the β value of 0.294, which means there is a positive effect of training on the application of the factors accounting for income tax which can be demonstrated by the increase in the training of the variable application of variable accounting for income tax will rise 0.294 assuming fixed values of other variables. This is supported by the statement Saputra (2002) training greatly affect a person's performance level, a growing number of workers doing the training will increase the performance of the workers. In the previous chapter it was mentioned that there are 19 companies or 24.05% of the total object of study in which the accounting staff of the company has never conducted training and 27 companies or 34.18% of the total object of study in which the company's accounting staff in training but never did 've never done training in SFAS 46. This indicates that the lack of awareness and willingness to undertake training of accounting staff regarding accounting, especially regarding SFAS 46. Such conditions will make the performance of the accounting staff disrupted resulting in low quality of the accounting staff. The training itself is very necessary to help employees improve their knowledge and ability to do his job. The statement in line with the opinion of Lopez (2008) which states that the implementation of the training is intended to get workers who have the knowledge, skills, abilities, and attitudes are good to run a particular job.

In addition, demographic data based on the position there are 11%, equivalent to 9 companies that fill the position as manager of the accounting department. This indicates that HR has done a lot of training, knowledge and understanding possessed meningkat and make the human resources manager of the accounting department at a company where the HR work. The more training undertaken by a person, the higher the level of understanding and knowledge that lead to office/position of the person can be increased. From some of the above it can be concluded that the factors that made the training of human resources, especially the training of SFAS 46 would affect the application of income tax accounting described in SFAS 46. In this case, the company should consider implementing training related to the field and work to their employees that the company will increase employee performance. The performance will affect the quality of the employee, because the higher the employee's performance will result in the quality of employees will increase.

Relationship work experience on Implementation of Accounting for Income Taxes

In the previous chapter it was mentioned that for the third hypothesis (H3) is considered to have a significant positive relationship between the experience factor working against the application of income tax accounting. The results showed that the effect of work experience on the application of income tax accounting has a t value of 2.019 is greater than the value of t table is 1.991 (t count > t table) and has a significance value of 0.047 is smaller than 0.05. Thus H3 is accepted that a significant effect of work experience on the application of income tax accounting. In addition, the results also showed that the β value of 0.324, which means there is positive the experience factor working against the application of income tax accounting can be demonstrated by the increase in the variable of work experience then the variable application of income tax accounting will increase the value of 0.324, assuming other variables remain. These results are in line with the statement Arfan and Edi (2009) which states that the more extensive work experience a person, the more skilled do the job and more perfect patterns of thinking and attitudes in acting to achieve its intended purpose. These results are also in line with the statement Huliah et al (2012) which states that the more extensive work experience a person, the more skilled do the job and more perfect patterns of thinking and attitudes in acting to achieve its intended purpose. This is supported by psychological theory Stimulus-response relationships were considers that the long experience to solve new problems. In the previous chapter has explained that the highest level of work experience is work experience of less than 2 years with a percentage of 29.1%, equivalent to a total of 23 companies from the object of research. The data indicates that the company is hiring accounting staff who do not have much experience. This will lead to the statement that the accounting staff who do not have much experience (<2 years) the knowledge and skills possessed in the company's accounting staff is still low compared to the company's accounting staff at other companies. The revelation is in line with the



statement of Saleh et al (2013) which states that the employee's performance is influenced by the work experience of the employee, the longer the employee experience will be easier to resolve suau product and the less experienced employees will affect the employee's ability to complete the production of a product. In addition, demographic data based on the position there is only 11%, equivalent to 9 companies that fill the position as manager of the accounting department. This indicates that the level of the manager, the human resources have a high work experience, knowledge and understanding to a greater job well. On the other hand, based on demographic data of age, by 55%, equivalent to 43 companies that have the human resources between the ages of 20-30 years. This indicates that the level of the HR work experience is low. Companies should regularly provide training to employees so that the human experience of growing so that level of ability and understanding of the work is increasing. Based on the above statement can be concluded that the longer the work experience in the field of human resource accounting, the greater the likelihood of human resources to understand and apply the accounting standards including SFAS 46 in the company's financial statement presentation. The company expected more considering doing work experience in the recruitment of new staff particularly accounting because the longer an employee has a work experience, the more knowledge and skill of the employees and the higher the quality of the employee-owned.

V. CONCLUSIONS AND RECOMMENDATIONS

Conclusion

This study was conducted to determine whether the quality of human resources through education variables, training, and work experience have a significant effect on the application of income tax accounting in construction company listed on the Primary Tax Office Palembang Ilir Barat. Based on the research conducted, it can be concluded that:

1. Results showed that the quality of human resources through education variables, training, and work experience simultaneously affect the application of accounting for income tax on listed construction company in Primary Tax Office Palembang Ilir Barat.
2. Variables of education, training, and work experience partial positive effect on the application of income tax accounting in listed construction company in Primary Tax Office Palembang Ilir Barat.
3. There are 11 companies that have accounting staff from the high school education. This indicates that the company's accounting staff on low quality and will have a negative impact on firm performance, especially in the field of accounting. The company is expected to be selective in their recruitment, especially in the field of accounting for all the work to be done can be completed accurately, quickly, and in accordance with applicable standards.
4. There are 19 companies or 24.05% of the total object of study in which the accounting staff of the company has never conducted training and 27 companies or 34.18% of the total object of study in which the accounting staff at the company have done the training but have never done training the SFAS 46. This indicates that the lack of awareness and willingness to undertake training of accounting staff regarding accounting, especially regarding SFAS 46. Companies should consider implementing training related to the field and work to karyawanya that the company will increase employee performance.
5. Highest level of work experience is work experience of less than 2 years with a percentage of 29.1%, equivalent to a total of 23 companies from the object of research. The data indicates that the company is hiring accounting staff who do not have much experience. The company expected more considering doing work experience in the recruitment of new staff particularly accounting.
6. Adjusted R2 value obtained on the sample of 79 companies in the amount of 0.460. This suggests that the major effect of independent variables: education, training, and work experience of the application of income tax accounting can be explained by the model equations for the remaining 46.0% and 54.0% influenced by factors outside the study.



Suggestion

Based on the above conclusions, there are some suggestions as follows:

1. Those companies are expected to be more selective in performing recruitment by considering the level of education, training I have ever attended, as well as work experience in accounting.
2. Those future studies should add some variables relating to the quality of human resources such as competence and motivation owned human resources can affect the application of income tax accounting.

Limitation

This study has limitations that may cause disruption to the results of this research study is confined to data from questionnaires distributed to construction companies registered at Primary Tax Office Palembang Ilir Barat so not describe the construction company in the city of Palembang as a whole.

References

- Ahmadi, Abu. 2002. *Psikologi Sosial Edisi Revisi*. Jakarta: Penerbit Rineka CIPTA.
- Arfan, Muhammad dan Edi Faisal. 2009. Pengaruh Masa Kerja, Jabatan, dan Jenjang Pendidikan Terhadap Tingkat Pemahaman Aparatur Pemerintah Tentang Prinsip-Prinsip *Good Governance* Di Pemerintah Kota Banda Aceh. *Jurnal Telaah & Riset Akuntansi*, Vol.2 No.1 Halaman 1-14.
- Badan Pusat Statistik. "Realisasi Penerimaan Negara (Milyar Rupiah), 2007-2013". Diambil pada tanggal 8 Oktober 2013 dari http://www.bps.go.id/tab_sub/vie.php?tabel=18&daftar=1&id_subyek=13
- Chaer, Abdul. 2003. *Psikolinguistik Kajian Teoritik*. Jakarta: Penerbit Rineka CIPTA.
- Darwanis dan Desi Dwi Mahyani. 2009. Pengaruh Kapasitas Sumber Daya Manusia, Pemanfaatan Tehnologi Informasi dan Pengendalian Intern Akuntansi Terhadap Keterandalan Pelaporan Keuangan Pemerintah Daerah. *Jurnal Telaah & Riset Akuntansi*, Vol. 2 No. 2 Halaman 133-151.
- Ghozali, Abbas. 2000. Pendidikan: Antara Investasi Manusia dan Alat Diskriminasi. *Jurnal Pendidikan dan Kebudayaan No.23 Tahun ke-6*. Mei.
- Ghozali, Imam. 2006. *Aplikasi Analisis Multivariat Dengan Program SPSS*. Jakarta : Badan Penerbit Universitas Diponegoro, Cetakan IV.
- Huliah, Abdurahman Rigel., Sifrid Pangemanan, Steven Tangkuman dan Novi Budiarmo. 2012. Pengaruh Sumber Daya Manusia dan Pemanfaatan Teknologi Informasi terhadap Keterandalan Pelaporan Keuangan pada Pemerintah Provinsi Sulawesi Utara. *Jurnal Riset Akuntansi dan Auditing*, Volume 3 – Nomor 2, Halaman 9-21.
- IkatanAkuntan Indonesia. 2012. *PSAK No.46*. Jakarta: SalembaEmpat.
- Karnoto, Mohamad. 2004. SDM, Kunci Menuju Prestasi. *Majalah Info Bank No.303*. Juni. Diambil pada tanggal 28 Nopember 2013 dari [http://www.bi.go.id/web/en/Tentang+BI/Perpustakaan/Periodikal/default.aspx?disp=Majalah%20Eksekutif%20\(1996-Feb%202009\)&idjs=1](http://www.bi.go.id/web/en/Tentang+BI/Perpustakaan/Periodikal/default.aspx?disp=Majalah%20Eksekutif%20(1996-Feb%202009)&idjs=1)
- Lubis, Khairul Akhir. 2008. Pengaruh Pelatihan dan Motivasi Kerja Terhadap Kinerja Karyawan PT Perkebunan Nusantara IV (Persero) Medan. *Tesis*. Sekolah Pascasarjana Universitas Sumatera Utara, Medan.
- Moekijat. 1991. *Latihan dan Pengembangan Sumbaer Daya Manusia*. Bandung: PT Mandar Maju.
- Republik Indonesia, *Undang-Undang Nomor 36 Tahun 2008 Tentang Perubahan Keempat Atas Undang-Undang Nomor 7 Tahun 1983 Tentang Pajak Penghasilan (PPH)*.
- Republik Indonesia. *Undang-Undang Nomor 13 Tahun 2003 Tentang Ketenagakerjaan*.
- Saleh, Muhammad., David PE Saerang, dan Ventje Ilat. 2013. Pengaruh Kualitas Sumber Daya Manusia, Pemanfaatan Teknologi Informasi dan Sistem Pengendalian Intern terhadap Keandalan dan Ketepatan Waktu Pelaporan Keuangan Perusahaan Dealer Mobil di Sulawesi Utara. *Jurnal Riset Akuntansi dan Auditing*, Volume 4 – Nomor 1, Halaman 54-67, ISSN : 2088-8899.
- Saputra, Abdul Djalil Indris. 2002. Membangun Manusia Indonesia. *Simposium Kebudayaan Indonesia – Malaysia VIII (SKIM 8)*. UKM. Bangi.



Siswanto. 2012. *Learning Curve*. WordPress. Diambil pada tanggal 3 Februari 2014 dari http://fe.uajy.net/fs/as/?page_id=6

Sumarni, Murti dan Wahyuni Salamah. 2005. *Metodologi Penelitian Bisnis*. Yogyakarta : Penerbit ANDI.
Tuasikal, Askam. 2007. Pengaruh Pemahaman Sistem Akuntansi dan Pengelolaan Keuangan Daerah terhadap Kinerja Satuan Kerja Perangkat Daerah. *Jurnal Akuntansi dan Keuangan Sektor Publik*, Vol.08, No. 01, Februari 2007.

Warisno. 2009. Faktor-faktor yang Mempengaruhi Kinerja Satuan Kerja Perangkat Daerah (SKPD) di Lingkungan Pemerintah Provinsi Jambi. *Tesis*. Sekolah Pascasarjana Universitas Sumatera Utara, Medan.
Winidyaningrum, Celviana dan Rahmawati. 2010. Pengaruh Sumber Daya Manusia Dan Pemanfaatan Teknologi Informasi Terhadap Keterandalan dan Ketepatanwaktuan Pelaporan Keuangan Pemerintah Daerah. *Simposium Nasional Akuntansi XIII Purwokerto*.



PENSION FUND INVESTMENT IN NIGERIA: ISLAMIC PERSPECTIVE

By

ADAM MUHAMMAD ABUBAKAR

Ph.D Student, Department of Islamic Jurisprudence,
Faculty of Islamic Sciences, Al-Madinah International University,
Shah-alam, Selangor, Malaysia.

adamsguru@yahoo.com,

Abstract

Pension and other social benefit matters have received significant attention for decades. The ways pension assets and benefits were managed and distributed to the target groups, are the major challenges associated with the pension schemes in many countries. Nigeria has experienced several reforms in Pension sector since 1951, through the public sector pension scheme, the establishment of National Provident Fund (NPF) of 1961, the Pension Decrees nos.102 and 103 of 1979 and the National Social Insurance Trust Fund (NSITF) Decree no.73 of 1993. During the past ten years, the Nigerian government has placed increasing emphasis on the new defined contributory (DC) pension scheme, in which employees and employers are expected to pay a certain percentage of the employees' monthly earnings to a retirement savings account (RSA), from which they will be drawing their pension benefits after disengagement from service, with the view of investing such fund by registered Pension Fund Administrators (PFAs) and Pension Fund Custodians (PFCs), under close supervision of Nigerian Pension Commission (PENCOM). This paper aims at giving an overview of Pension Fund investment under this contributory pension scheme, by assessing its provisions, in the light of the general principles of Islamic economics. It also highlights some areas that contradict Islamic teachings and provides alternatives from Islamic perspectives.

Keywords: Nigeria, Shari'a, Investment, and Pension Fund.

Introduction

Background of the Study

According to (Adams, 2005) pension is the amount paid by government or company to an employee after working for some specific period of time, considered too old or ill to work or have reached the statutory age of retirement. It is equally seen as the monthly sum paid to a retired officer until death because the officer has worked with the organization paying the sum.

Pension funds contribute directly and indirectly to the economic growth of countries worldwide; hence, the importance of pension fund to the economic development of any economy cannot be overemphasized. The global indices indicate that pension assets are playing an important role in mobilizing savings for investment in the critical sectors (Njuguna, 2010). According to (Umar, 2012) Pension funds add value to the world economies through direct contribution to the GDP, accumulation of savings, financial market development, reducing old-age poverty and acting as consumers of financial services.



In Nigeria prior to 2004 Pension Reform, the pension system was characterized with many problems, which include: unsustainable pension liabilities, lack of adequate and timely budgetary provision coupled with rising life expectancy, increasing number of employers, poor implementation of pension scheme in the private sector due to inadequate supervision and regulation, among others (Adejoh, 2013).

These problems necessitated a transformation in the Nigerian pension sector, which eventually gave birth to the pension reform Act of 2004, which established a uniform contributory; private sector managed and fully funded pension system for both the public and private sector of the country. It also established a large capital pool that invests funds for future pension entitlements of beneficiaries to ensure that value is added to pension fund through financial intermediation, which affect financial markets in particular and economic activity in general (Ahmed, 2006).

Statement of the Problem

The new Pension Reform Act 2004 provides that pension fund should be invested by a licenced pension fund administrator, in a conventional manner of investment, which includes: bonds, bills and other securities issued or guaranteed by the Federal Government and the Central Bank of Nigeria; debentures, redeemable preference shares and other debt instruments issued by registered corporate entities (PRA 2004).

It is apparent that most of the above mentioned means of investment are not Sharia compliant means, and there is overwhelming majority of Muslims in Nigeria who want to have their source of livelihood after retirement invested in a sharia compliant business. This paper will analyse the investment provisions of Pension Reform act from Islamic perspective, highlight the areas that contradict Islamic teachings and provide Sharia compliant investment alternatives.

Pension Schemes In Nigeria: A Historical Overview

Old Pension schemes In Nigeria

The history of pension system in Nigeria dates back to the year 1951. According to Balogun (2006), Pension Ordinance of 1951 was the first legislative act on pension in Nigeria, which had a retroactive effect from 1st January 1946, while The National Provident Fund (NPF) of 1961 was the first legislation enacted to address pension matters of private organizations.

Subsequently, in 1979, the Pension Act No.102 and the Armed Forces Pension Act No. 103 were instituted. In 1987, the police and other government agencies pension scheme was established under Pension Act No.75 of 1987. Similarly, the Local Government Staff Pension Board was established in the same year, to take care of pension matters among local government employees. While in 1993, the National Social Insurance Trust Fund (NSITF) scheme was established to replace the defunct NPF scheme, with effect from 1st July, 1994, to address pension and retirement issues in the private sector (Ahmed, 2006).

According to (Barrow, 2008), these Decrees remained the operative laws on public service and military pension in Nigeria until July, 2004, though there were several government circulars and regulations issued to alter their provisions and implementations. It should also be noted that pension schemes in Nigeria over these years have always relied upon budgetary allocations, thereby creating bottlenecks, due to delay or lack of payment after retirement.

The Nigerian Pension Reform Act 2004

According to Blake (2003), Pension reform is not a new issue in any part of the world, since it is usually a continuous process especially with the ever-changing economic and political processes witnessed

worldwide. In Nigeria, the Pension Reform Act of 2004 is the most recent legislation of pension, which aimed at addressing the associated problems of the old Pension Systems. It also established a uniform Pension System for both the public and private sectors, and provided a contributory pension scheme; whereas both the employees and employers are to contribute a minimum of 7.5 percent of the employee's basic salary respectively, so the total minimum monthly contribution of a typical employee is 15 percent of his/her basic salary (PRA,2004). According to the Act, the key objectives of the new scheme are:

To ensure that every person who has worked in either the public or private sector receives his retirement benefits as and when due.

To assist improvident individuals by ensuring that they save to cater for their livelihood during old age.

To establish a uniform set of rules and regulations for the administration and payment of retirement benefits in both the public and private sectors, and

To stem the growth of outstanding pension liabilities.

To secure compliance and promote wider coverage.

Under this Act, the employee opens an account known as 'Retirement Savings Account in his name with a Pension Fund Administrator of his choice. This individual account belongs to the employee and will remain with him throughout his lifetime. He may change employers or pension fund administrators but the account remains the same. The employee may only withdraw from this account at the age of 50 or upon retirement thereafter (PRA, 2004).

Pension Fund Management Under Pension Reform Act.

The PRA, 2004 provided a Contributory Pension Scheme that is fully funded, and privately managed by Pension Fund Administrators, with the pension funds assets held by Pension Fund Custodians, under closed supervision of National Pension Commission (Barrow, 2008). Therefore, the major operators under the scheme are the National Pension Commission (PenCom), Pension Fund Administrators (PFAs), Pension Fund Custodians (PFCs) and Closed Pension Fund Administrators (CPFAs).

The National Pension Commission (PenCom)

The National Pension Commission (PenCom) was established to regulate, supervise and ensure an effective administration of pension matters. It is for the first time in the history of Nigeria that a single authority has been established to regulate all pension matters in the country. Having identified that one of the reasons for the failure of previous schemes was lack of strict and effective regulations, the new scheme has mandated (PenCom) to carry out the following functions inter alia:

- To establish standard rules for the management of pension funds.
- To approve license and regulate PFAs, PFCs and CPFAs.
- To manage national data bank on pension.
- To ensure constant payment and remittance of contributions.
- To impose sanctions or fines on erring employers, PFAs, PFCs and CPFAs.
- To investigate any malpractice by any party involved in the management of pension funds, and
- To ensure that beneficiaries of retirement savings accounts (RSAs) are paid as and when due (PRA, 2004).



The Nigerian Pension Fund Administrators (PFAs)

The new pension scheme requires pension funds to be privately managed by licensed Pension Fund Administrators to invest and manage the pension funds in accordance with the provisions of the Pension Reform Act 2004. Adegbayi (2005) has identified that the roles of PFAs are to open RSA for all employees registered by it with a Personal Identification Number (PIN); invest and manage the Fund and assets; Calculate annuities; and pay Retirement Benefits.

The act also provided that the PFA must be a limited liability company whose sole object is the management of pension funds; and must have a paid up share capital of N150, 000,000 (approximately \$1,000,000USD).

According to (PenCom, 2014) currently, there are 20 registered and licensed Pension Fund Administrators in the country.

The Nigerian Pension Fund Custodians (PFCs)

The Pension Fund Custodians (PFCs) are responsible for the warehousing of the pension fund assets, since the PFAs are not allowed to hold the pension fund assets. Hence, the two interlock and act as a grid against financial impropriety. The Custodian must be a licensed financial institution and have a minimum net worth of N5, 000, 000, 000 (approximately \$30,000,000USD) and a total balance sheet of not below N125, 000,000,000 (approximately \$800,000,000USD).

According to Adejoh, (2013), the primary functions of PFCs are: to receive and hold the Fund upon trust for Contributors and Beneficiaries; Settle investment transactions on behalf of the PFAs; provide independent reports to the Pension Commission on Fund assets and Undertake statistical analysis on the investment and returns on behalf of the Pension Commission and the PFAs.

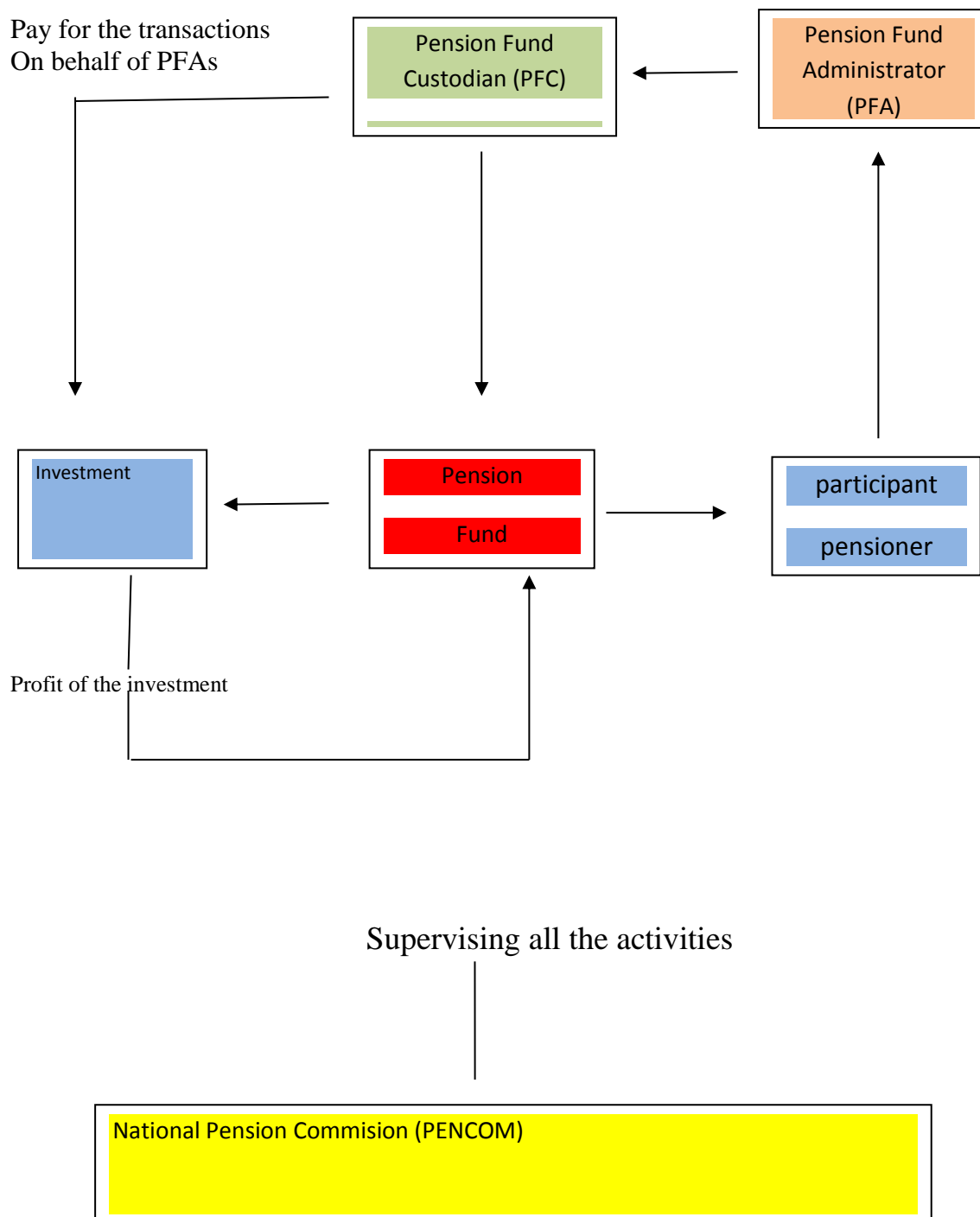
The Closed Pension Fund Administrators (CPFAs)

The Closed Pension Fund Administrators (CPFAs) are specifically established by the PRA, for companies with strong financial standing to manage their pension funds either directly or through a wholly owned subsidiary of such company dedicated exclusively for the management of pension fund. Currently, there are about seven CPFAs owned mostly by multinational companies (Adejoh, 2013).



Figure 1

The organizational structure of the Pension Fund Management in Nigeria based on the new Pension Reform act



The Investment Of Pension Fund In Nigeria

The PRA, 2004, specifically spelt out that all contributions made by employees and employers should be invested by a licensed pension fund administrator, in order to avoid the illiquidity and unsustainability that plagued the erstwhile-defined benefit system. The investment should be carried out with the objectives of safety and maintenance of fair returns on pension funds amount invested. Adegbayi, (2005), emphasized that safety here ties in with the safety of the principal contribution, which must be sufficient to provide guaranteed minimum pension after certain years of contribution.

Primarily, pension fund assets may be invested in the following categories of investment:

- Federal Government Bonds, Treasury Bills and related securities
- Quoted Bonds and debt instruments
- Quoted stocks and shares
- Bank deposits and securities
- Quoted closed end Funds or hybrid investments
- Quoted unitized investments
- Real Estate investments
- Other investment prescribed by the Pension Commission

Similarly, certain investments are not permitted, these include Own or Affiliates Shares and Securities, therefore, pension fund assets cannot be sold to nor purchased by, nor loaned to any one directly or indirectly connected with a PFA or PFC whether by familiar or business relationship (Adegbayi, 2005).

The Sharia Compliant Pension Fund Investment In Nigeria

The basis of Sharia Compliant investment

Sharia compliant investment is an alternative form of investment that is based on profit and loss sharing in line with the Islamic values. Sanusi, (2011) observed that although the Islamic financial system is based on a religious law, it is nevertheless, not a religious product or service that is the exclusive preserve of people of a particular faith or religion. Hence, it is universally accessible to and enjoyed by people of diverse religious persuasions or ethical beliefs across the globe.

According to Rano, (2012) the Islamic system of finance is coveted for its prohibition of interest, despising uncertainty and denouncing speculation. It is also admired for fostering economic development, social progress and distributive justice, which make it more concerned with the viability of business proposal and profitability.

Generally, the Sharia compliant investment operates entirely on the principles of shari'ah law, whose main traditional sources were the Holy Qur'an, Sunnah of the Holy Prophet (traditions), Ijma' (consensus of Ulama) and Qiyas (Analogical deduction). The Holy Qur'an categorically condemns all forms of transaction, which involves giving or taking of usury, or interest, Allah said:

"O ye who believe, fear Allah, and give up what remains of your demand for usury, if ye are indeed believers. If ye do not, take notice of war from Allah and His messenger: but if ye turn back, ye shall have your capital sums; deal not unjustly, and ye shall not be dealt with unjustly". (Chapter 2 verses 278-279).

According to Al-Omar, et al. (1996) the four main principles of Islamic investment are:

- a) There must be some risk, whether funds are used in commercial or productive venture.
- b) All funds should preferably finance socially and ethically productive activity.
- c) Financial risk must lie solely with the lender of the capital and not with the manager or agent who works with the capital.
- d) Interest is forbidden in that it is a predetermined, fixed sum owed to the lender irrespective of the outcome of the business venture in which the fund is used.

Islam also prohibits other forms of arrangements or conditions associated with the execution of business contract which involve elements of Gharar (uncertainty), gambling, speculation, deceit, etc. (Zineldin, 1990).

The Instruments of Sharia Compliant Pension Fund Investment

The Islamic system of finance uses a number of instruments that can be considered as an alternative channel of pension fund investment based on the general principles of sharia, among them are:

Murabahah (Cost-Plus Sale Contract)

A Murabahah transaction is a sale at a stated profit. In a Murabahah transaction, the Investor purchases an asset from a third party and sell it to the client at a stated profit on a spot or deferred payment basis. In this way, the client can buy something without taking an interest-based loan.

Ijarah (Lease)

An ijarah is an Islamic lease. The Investor purchases an asset and leases it to a client for fixed monthly payments. It may include an option for the lessee to buy the asset at the end of the lease, which is a way for Islamic investment to provide finance for ownership of goods and services.

Mudarabah (Silent Partnership)

A Mudarabah transaction is an investment partnership which implies contract between an investor (or financier) and an entrepreneur or investment manager known as the Mudarib. In this contract, risk and rewards are shared. In the case of a profit, both parties receive their agreed-upon share of the profit. In the case of a loss, the investor bears any loss of capital while the Mudarib loses his time and effort.

Salam (Forward Trade Contract)

Salam contract is a sale where the seller undertakes to supply some specific goods to the buyer at a future date that is specified in exchange of an advanced price fully paid at spot. This mode of financing is widely used to finance the agricultural sector.

Istisna' (Partnership in Manufacturing)

This is a mode of financing where the commodity involved is manufactured to the specifications of the purchaser. It is widely used in the housing finance sector, where the client seeks finance for the construction of a house. The financier may undertake to construct the house on a specified land either belonging to the client or purchased by the financier, based on Istisna', with payment fixed in whatever manner the parties may agree upon. It is also widely used in infrastructure finance.

Musharakah (Equity Partnership)

This involves partners providing funds for a venture, with profits shared according to an agreed ratio, and the loss is borne by them in accordance with their capital contributions.



The General Framework of Sharia Compliant Pension Fund Investment In Nigeria

According to Rano, (2012) the Nigeria's financial industry is wholly conventional for over a century, whereas all the financial institutions are based on the principle of taking and offering of interest. While the position of Islam on the issue of interest is very clear as enunciated in the aforementioned Qur'anic verse. Therefore, only investment operations that are *halal* or shari'ah compliant are considered under Islamic Pension Fund Investment system.

Contemporarily, this can be realized in Nigerian Pension Sector through the following means:

Establishment of a Dedicated IPFA

The establishment of a dedicated Islamic Pension Fund Administrator (IPFA) means to establish a full pledge Sharia compliant pension fund administrator, which operates entirely based on profit and loss sharing in accordance with the principles of shari'ah and its value. Therefore, it will not accept any business that is not Sharia compliant such as casinos, alcoholic industries, proceeds from prostitution, sale of wine, etc.

Since the PFAs are not allowed to hold the pension fund assets, based on the provisions of Pension Reform Act, (2004), there is need for the establishment of an Islamic Pension Fund Custodian (IPFC), to ensure Sharia compliant warehousing of the pension fund assets. Hence, all contributions under IPFA should be under the custody of a full pledge Sharia compliant pension fund custodian, such as Jaiz Bank Nigeria, PLC.

Establishment of Islamic Pension Investment Window operation:

Establishment of Islamic Pension Investment Window operation refers to an investment model in which conventional pension fund administrators (PFAs) offer an interest-free Pension Fund Investment products and services from their existing network. To ensure a sharia compliant operation of such windows, the following conditions must be fulfilled:

- Establishment of a dedicated Islamic Pension Fund Administration (IPFA) division to oversee the overall window operations of the institution and its compliance with the principles guiding the sharia compliant investment;
- Segregation of Islamic Pension Investment funds from conventional pension funds;
- Separate disclosure of the Islamic Pension Investment financial statements;
- Submission of separate statistical and prudential reports of Islamic Pension Investment to regulatory authorities and the customers as well.

It is worthy of note that since the Nigeria's financial industry has been wholly conventional for many decades, Islamic Pension Fund Administrators (IPFA) in Nigeria, could because of the non-compliant nature of the business environment, take advantage of equally competitive investments opportunities around the globe; especially Middle East, South Asian counties, Europe, and the United States. Similarly, there are also numerous investment opportunities and partnership arrangements for both private sector

and governments at all levels existing at the Islamic Development Bank (IDB), International Islamic Monetary Fund (IIMF), OIC countries, etc. (Sanusi, 2011).

Consequently, the emergence of Islamic pension fund investment in Nigeria will no doubt help to cajole and douse the apathy among public to accept the pension system that now suit their preferences and recognize their religious values and beliefs. Hence, it will remedy the issue of non-compliance of the public to the new contributory pension scheme, or at least reduce it to some extent.

Conclusion

The importance of pension provision will continue to grow, as individuals begin to place less reliance on family to look after them in old age and begin to face the reality that they need to look after themselves by building a nest egg for the future. This research discovered that the new contributory pension scheme established by the Nigerian Reform Act, (2004), has helped in reducing the problem associated with the old pension schemes; and that effective and sound investment and management of pension fund has a tremendous impact on the individuals, private sector and the country's economy at large.

The study also discovered that the success of the pension reforms largely depends on the sincerity, collaboration and commitment of all stake holders like government that sets out the regulatory framework; the regulator PENCUM; financial institutions who manage and administer contributions; individuals who pay and employers who must also contribute for their employees.

It also highlighted that there are some areas in the Nigerian contributory pension scheme that contradict Islamic teachings, especially channels of pension fund investment, which characterized to be solely secular and conventional in nature.

Finally, the study proves the universality and flexibility nature of Islam, by providing alternative Sharia compliant forms of investment, as well as the general framework for the establishment of both Islamic Pension Fund Administrator (IPFA) and Islamic Pension Fund Custodian (IPFC).

References

- Adams, R.A. (2005). *Public Sector Accounting and Finance*, Lagos, Corporate Publisher Ventures.
- Adegbayi, A (2005). "Pension Industry Development in Nigeria – The thrust of the Pension Reform Act 2004". www.leadway.com
- Adejoh, E. (2013). 'An Assessment of the Impact of Contributory Pension Scheme to Nigerian Economic Development' in *Global Journal of Management and Business Research*, Vol. 13 No.1 USA. P2
- Barrow, G. (2008). *Pension Fund Administration in Nigeria*. Abuja, Nigeria: Pen and Pages Ltd.
- Blake, D. (2003). *The United Kingdom Pension Scheme in Nigeria*, Pension Institute, Bareback College, University of London.
- Federal Republic of Nigeria (2004). *Pension Reform Act*.



Njuguna, A. G. (2010). *Strategies to Improve Pension Fund Efficiency in Kenya*. An Unpublished Ph.D Thesis of Nelson Mandela Metropolitan University, Port Elizabeth.

Sanusi, L.S. (2011). *Islamic Finance in Nigeria: Issues and Challenges: A Lecture delivered At Markfield institute of higher education (mihe), leicester, uk* By Sanusi lamido sanusi (con) Governor, central bank of nigeria 17 june 2011.

Umar, G. (2012). *Contributory Pension System as a Tool for Economic Growth in Nigeria* International Journal of Business and Behavioral Sciences Vol. 2, No.8; August 2012.

Zineldin, M. (1990). *The Economic of Money and Banking*: Almqvist & Wiksell, Stockholm, Sweden



Kajian Penggunaan Tajuk dalam Penyata Kewangan di Malaysia

MOHD NOOR AZLI BIN ALI KHAN
 Jabatan Perakaunan dan Kewangan
 Fakulti Pengurusan
 Universiti Teknologi Malaysia
 81310 UTM Johor Bahru, Johor, MALAYSIA
m-nazli@utm.my

Abstrak

Kajian ini bertujuan untuk mengkaji penggunaan tajuk yang digunakan dalam penyata kewangan berbahasa Melayu bagi syarikat yang tersenarai di Bursa Malaysia. Kajian dijalankan berpandukan kepada *Financial Reporting Standards* (FRS) 101 bagi Pembentangan Pelaporan Kewangan syarikat. Penelitian dibuat ke atas syarikat bagi tempoh dua belas tahun bermula dari tahun 2001 hingga 2012. Populasi kajian diambil daripada jumlah syarikat yang tersenarai di Papan Utama Bursa Malaysia pada tahun 2012 iaitu sebanyak 809 buah syarikat. Sampel kajian diambil sebanyak 263 buah syarikat daripada jumlah populasi kajian. Sampel kajian yang diambil perlulah mempunyai maklumat dalam penyata kewangan menggunakan Bahasa Melayu. Penelitian terperinci dilakukan terhadap penggunaan tajuk yang digunakan dalam Penyata Kedudukan Kewangan, Penyata Kewangan Komprehensif, Penyata Perubahan Ekuiti dan Penyata Aliran Tunai. Hasil kajian mendapati bahawa penggunaan tajuk dalam penyata kewangan majoritinya adalah seragam. Kajian yang dijalankan ini adalah penting kepada kajian lanjutan berkaitan pelaporan tajuk dalam penyata kewangan berbahasa Melayu sebagai perantara di dalam penyampaian maklumat perakaunan kepada pihak yang berkepentingan. Implikasi dan cadangan kajian turut dibincangkan dalam kajian ini.

Kata kunci: *Financial Reporting Standards* (FRS), Bahasa Melayu, Bursa Malaysia, Laporan Tahunan, Penyata Kewangan.

PENGENALAN

Malaysia merupakan antara negara yang tersenarai di antara negara paling berdaya saing. Sebagai contoh sebuah negara berdaya saing, Malaysia tidak ketinggalan dalam amalan pelaporan kewangan yang diaplikasikan di seluruh dunia. Lebih dari 7000 syarikat yang berdaftar di Eropah, Australia, Singapura dan Hong Kong melaporkan prestasi kewangan mereka di bawah *International Financial Reporting Standards* (IFRS). Corak pembentangan penyata kewangan berbeza disebabkan oleh perbezaan dari segi piawaian yang diguna pakai dalam laporan tahunan negara masing-masing. Oleh demikian, dalam memastikan wujudnya amalan terbaik dalam urusan tadbir korporat di Malaysia, Lembaga Piawaian Perakaunan Malaysia (LPPM) telah memperkenalkan piawaian baru bagi penyediaan penyata kewangan, pada peringkat awal pengenalan tempoh diberi dalam masa empat tahun, sebelum semakan piawaian dibuat. Di Malaysia, usaha dalam menyeragamkan penggunaan tajuk penyata kewangan khususnya dalam perakaunan masih belum giat dijalankan dan tiada usaha untuk mengkaji keseragaman secara ilmiah dibuat. Usaha dalam menyeragamkan penggunaan tajuk penyata kewangan ini hanya dilakukan oleh Suruhanjaya Sekuriti yang menghantar wakilnya untuk menghadiri bengkel anjuran Dewan Bahasa dan Pustaka (DBP) untuk membincang, mengesah dan menyeragamkan penggunaan terminologi dan istilah berkaitan ekonomi, perakaunan, perbankan, insurans, perniagaan, percukaian, perdagangan dan pelaburan. Setiap syarikat sama ada sendirian berhad atau berhad di Malaysia yang berdaftar di bawah Akta Syarikat 1965 perlu mengeluarkan satu laporan tahunan yang menjelaskan tentang operasi syarikat



bagi kepentingan pihak-pihak yang tertentu seperti pelabur, pemegang saham, pendidik, penganalisis kewangan dan pihak berkepentingan yang lain. Aspek yang perlu dititikberatkan adalah ianya mudah dibaca dan difahami oleh pihak yang memerlukannya.

Kebanyakan laporan tahunan yang dikeluarkan mengekalkan ciri tidak dapat menarik perhatian para pengguna di samping bahasa yang digunakan juga sukar untuk difahami. Perakaunan menggunakan nombor telah menjadi satu tradisi bagi menyampaikan maklumat. Ini bermakna, nombor adalah lebih penting daripada istilah kerana nombor boleh menggambarkan maksud yang hendak dinyatakan (Barth, 2008). Pihak pengurusan perlu menyediakan penyata kewangan yang mengandungi maklumat yang relevan bagi membolehkan pengguna maklumat membuat keputusan (Barth, 2008). Oleh itu, wujudnya persoalan tentang sejauh mana isu kefahaman ini dimaksudkan. Ini disebabkan oleh di dalam konteks komunikasi, sesuatu perhubungan yang berkesan berlaku apabila mesej yang dihantar oleh pihak penghantar diterima oleh pihak penerima dan dapat ditafsir seperti yang diharapkan oleh pihak penghantar. Walaupun komunikasi ini agak memakan masa untuk sampai ke pihak yang berkepentingan, namun laporan tahunan mengandungi data yang komprehensif berkaitan pencapaian syarikat pada masa lalu serta menyediakan maklumat untuk pengesahan, semakan semula dan pengetahuan kepada pengguna berbanding kepentingan mereka dalam laporan tahunan tersebut. Selain itu, ia bersifat '*neutral*' iaitu tidak menyebelahi mana-mana pihak dan maklumat yang cukup dan lengkap (Porter & Norton, 2010).

Di dalam teori agensi, terdapat ikatan antara pemegang saham dan pihak pengurusan korporat. Ini dikenali sebagai kontrak pekerjaan yang bermaksud pihak pengurusan korporat perlulah melaporkan aktiviti syarikat secara tepat dan saksama (Scott, 1997). Oleh yang demikian, laporan tahunan perlu disediakan secara telus, tepat, lengkap dan mudah difahami (Epstein, Barry & Eva, 2008). Kajian sebelum ini mendapati bahawa dua komponen dalam laporan tahunan adalah istilah dan nombor (Aisbitt & Nobes, 2001). Sekiranya berlaku ketidakfahaman, mungkin disebabkan oleh tahap komunikasi pengguna yang berbeza (Ali, Chen & Radhakrishnan, 2007). Walau bagaimanapun, sepanjang perkembangan FRS di Malaysia, didapati hanya segelintir pengkaji yang menumpukan kepada piawaian laporan tahunan ini. Hasil kajian mendapati, masa yang diberikan kepada syarikat untuk menerima piawaian ini adalah terhad (Yen, Hirst & Hopkins, 2007). Namun begitu, banyak kajian yang telah dijalankan dalam mengenal pasti hubung kait terminologi, bahasa, istilah serta piawaian perakaunan yang digunakan, namun masih ada lagi faktor lain yang perlu diberi perhatian. Kebanyakan laporan tahunan yang dikeluarkan mengekalkan ciri tidak dapat menarik perhatian para pengguna di samping terminologi yang digunakan juga sukar untuk difahami (Archer & McLeay, 1991). Ada juga pihak yang mempertikaikan keberkesanan laporan tahunan ini sebagai medium komunikasi. penggunaan terminologi dan istilah yang tidak seragam boleh menyebabkan nombor yang tertera tidak dapat memberikan makna dan gambaran sebenar terhadap maklumat yang disampaikan (Barth, Landsman & Lang, 2007).

Kajian ini dijalankan adalah kerana di Malaysia sehingga kini masih belum mempunyai satu piawaian penggunaan tajuk penyata kewangan di dalam Bahasa Melayu yang boleh diterima pakai umum. Di samping itu, kajian berkaitan penggunaan tajuk penyata kewangan di dalam Bahasa Melayu masih kurang dijalankan oleh pihak yang bertanggungjawab di Malaysia. Penggunaan tajuk penyata kewangan ini juga tidak mempunyai penguatkuasaan undang-undang yang sewajarnya. Tajuk penyata kewangan ini juga diharapkan dapat diterima pakai oleh pihak penggubal piawaian perakaunan di Malaysia. Hasil daripada kajian ini diharapkan akan dapat menjadi permulaan kepada syarikat yang mengeluarkan laporan tahunan dengan menggunakan tajuk penyata kewangan terutamanya di dalam Bahasa Melayu. Objektif kajian ini adalah untuk mengkaji sama ada penggunaan tajuk penyata kewangan adalah selaras dengan apa yang diutarakan oleh *Malaysian Financial Reporting Standards*.

Artikel ini disusun seperti berikut: bahagian seterusnya akan membincangkan tentang latar belakang kajian yang dijalankan; diikuti dengan kajian literatur yang menyeluruh. Bahagian seterusnya pula membincangkan tentang metodologi kajian serta dapatan kajian. Akhir sekali, artikel ini berakhir dengan kesimpulan daripada kajian yang dijalankan.

LATAR BELAKANG KAJIAN

Persembahan penyata kewangan merupakan salah satu alternatif syarikat melaporkan laporan tahunan (Richardson, Tuna & Wu, 2002). Usaha untuk mencapai persembahan penyata kewangan yang adil, aset, liabiliti, pendapatan dan perbelanjaan perlu diiktiraf dan jika perlu, pelaporan tambahan juga perlu dilaporkan (Daske, Hail, Leuz & Verdi, 2008). MASB 1 dibangunkan berdasarkan IFRS atau *International Accounting Standards* (IAS 1) yang telah disemak. Pembentangan Penyata Kewangan ini dikeluarkan oleh Lembaga Piawaian Perakaunan Antarabangsa (Hassan & Salleh, 2010). LPPM telah menerbitkan piawaian perakaunan dalam Bahasa Melayu kepada syarikat awam dalam menyediakan laporan tahunan mereka. LPPM tidak mewajibkan syarikat untuk menerima pakai tajuk yang telah dicadangkan. Menguasai kemahiran persembahan dapat meningkatkan proses memindahkan idea, bahkan dapat menentukan kaedah satu pihak berupaya menguasai pihak yang lain dan juga dapat memastikan proses komunikasi dua hala sentiasa berterusan (Maines & McDaniel, 2000). Tujuan laporan tahunan adalah untuk memberi maklumat tentang kedudukan kewangan, prestasi dan perubahan kedudukan kewangan syarikat yang berguna untuk pengguna bagi membuat sebarang keputusan (Feltham, Indjejikian & Nanda, 2006).

Sumbangan praktikal dalam mengenal pasti faktor tertentu di dalam reka bentuk persembahan laporan tahunan syarikat, ini adalah bertepatan dengan tujuan PPK 101 yang turut menerapkan keperluan keseluruhan persembahan, panduan berstruktur dan keperluan minimum untuk isi kandungan penyata kewangan berdasarkan FRS 101₂₀₀₅ Para 1 (Booth & Schulz, 1995). Kajian yang dijalankan ini memberikan tumpuan terhadap penggunaan terminologi dan istilah perakaunan yang terdapat di dalam pembentangan penyata kedudukan kewangan, penyata kewangan komprehensif, penyata aliran tunai serta penyata perubahan ekuiti. Kajian ini diharapkan dapat menjadi titik permulaan kepada kajian-kajian pada masa akan datang terhadap penekanan Bahasa Melayu dalam laporan tahunan syarikat terutamanya bagi istilah dan juga terminologi perakaunan. Hal ini dapat memudahkan pengguna untuk lebih memahami pelaporan kewangan yang disediakan oleh syarikat di Malaysia. Setiap komponen penyata kewangan perlu dikenal pasti dengan jelas.

Selain daripada itu, maklumat yang penting perlu dipaparkan dan diulang sekiranya perlu, bertujuan memberi pemahaman yang tepat terhadap maklumat yang dipersembahkan (Van, 1993). Thompson (2008) menyatakan bahawa syarikat perlulah telus dan jelas dalam membuat pelaporan penyata kewangan. Piawaian dan nasihat bebas diperkukuhkan lagi melalui *Guidelines on Offer Documentation of the Malaysian Code on Take-overs and Mergers* yang kini masih diperkemas lagi (Holthausen & Watts, 2001). Bahagian seterusnya menerangkan tentang pencapaian serta penumpuan daripada kajian lepas yang menjadi asas panduan kepada kajian ini.

KAJIAN LEPAS

Berdasarkan kajian yang telah dijalankan, kajian yang dijalankan menyeluruh membincangkan tentang penerimaan negara yang berbeza terhadap laporan tahunan yang dilaporkan. Dari segi laporan tahunan dan juga kepentingannya yang paling utama adalah mengandungi maklumat jadual, gambarajah, graf, penceritaan, nombor dan istilah (Courtis, 1995), kesan komunikasi pihak penyedia laporan tahunan dengan pengguna laporan tahunan (Hopkin, 1996) dan juga piawaian pembentangan laporan tahunan (Botoson, 2004), memudahkan proses pengauditan (Booth & Schulz, 1995), medium komunikasi (Alexander, 1993), pencapaian syarikat (Courtis, 1998), laporan tahunan sukar difahami (Archer & McLeay, 1991). Kebanyakan pengkaji melakukan kajian terhadap beberapa negara mengenai laporan tahunan yang disediakan ke atas negara seperti China (Belkaoui & Picur, 1991), Jordan (Bartov, Goldberg & Kim, 2005), Eropah (Baldwin, Dull & Graham, 2003), Amerika Syarikat (Hjarvard, 2003), Asia

(Globerman, Peng & Shapiro, 2011), Perancis, Belanda (Parker, 1994), Jepun (Okada, 2008) dan Malaysia (Ali Khan & Mohd Zaini, 2012).

Keperluan undang-undang adalah penting dalam penyediaan laporan tahunan. Kajian lepas banyak membincangkan tentang kaedah persembahan laporan tahunan (Hirst & Hopkins, 1998), pematuhan asas piawaian (Parker, 1994; Jeanjean & Stolowy, 2008; Benston, 1982; Bartov, Goldberg & Kim, 2005; Geoff, 2004), etika perakaunan (Belkaoui & Picur, 1991), maklumat yang lengkap (Porter & Norton, 2010), ICAEW, IASB (Baldwin, Dull & Graham, 2003) dan sistem maklumat (Beretta & Bozzolan, 2004; Carter & Van, 2006; Baldwin, Dull & Graham, 2003). Berdasarkan kajian konsep dan prinsip penyata kewangan (Hein, Beuren & Klann, 2008), ianya terbahagi kepada kajian pelaporan berasaskan nilai saksama (Healy & Perry, 2000; Gerard, 2011; Mohd Iskandar & Basnan, 2002; Bradshaw, Bushee & Miller, 2004; Hooi, Tee & Lim, 2003). Selain itu kajian juga membincangkan tentang istilah perakaunan dalam penyata kewangan (Iselin, 1989; Chen & Sami, 2008; Chan & Seow, 1996; Jones, 1996; Parker, 1994; Aisbitt & Nobes, 2001; Brown, 1995; Covrig, DeFond & Hung, 2007; Hjarvard, 2003). Penggunaan istilah dan terminologi dalam komunikasi serta tanggungjawab korporat (Davidson & Chrisman, 1993; Parker, 1994; Craven & Marston, 1997; Peng & Bewley, 2010; Jeanjean & Stolowy, 2008; Cuijper & Buijink, 2005; Melis & Carta, 2010; Kosmala, 2003; Awang, 1995; Young, 2003; Sun, 2007; Evans, 2004; Brennan, Guillaumon-Saorin & Pierce, 2009; Carter & Auken, 2006). Peranan laporan tahunan adalah penting kerana mempunyai kaitan dengan pihak yang berkepentingan (Ashbaugh & Pincus, 2001), kontrak pekerjaan (Scott, 1997), kebolehbacaan (Epstein, Barry & Eva, 2008), alat komunikasi (Young, 2003), pembuatan keputusan syarikat (Ball, Robin & Wu, 2003) dan pengawasan ke atas sumber syarikat (Barker, 1998).

Seterusnya komponen penyata kewangan dibincangkan dalam kajian (Aisbitt & Nobes, 2001; Barth, Landsman & Lang, 2007; Ali, Chen & Radhakrishnan, 2007). Pihak penyedia laporan tahunan perlu mengatasi masalah penggunaan bahasa dan istilah yang digunakan supaya dapat memudahkan semua pihak mendapat tafsiran yang sama (Beretta & Bozzolan, 2004; Carter & Van, 2006; Baldwin, Dull & Graham, 2003). Penggunaan istilah dan terminologi sebenarnya memberikan kesan terhadap pemahaman di antara pihak penyedia dengan pihak pengguna laporan tahunan (Maines & McDaniel, 2000; Mills, 1989). Kajian sebelum ini ada membuktikan terdapat perbezaan dalam istilah yang digunakan di negara seperti United Kingdom dan Amerika Syarikat (Aisbitt & Nobes, 2001; Barth, Landsman & Lang, 2007; Ali, Chen & Radhakrishnan, 2007). Kajian berpendapat bahawa perubahan dalam istilah dan terminologi berpunca daripada perubahan dalam erti, dan masa perubahan, tetapi khususnya sebab perubahan boleh menarik minat kepada sejarah, kerana pemeriksaan yang terperinci boleh mencegah salah tafsir kepada sesuatu sumber bahan sejarah dan juga memberi maklumat yang berguna kepada peralihan sosio-ekonomi, politik atau ideologi proses dan hubungan kuasa (Archer & McLeay, 1991). Seterusnya bagi asas perakaunan akruan dan nilai semasa atau bukan semasa dijalankan oleh (Beattie, Brown & Ewers, 1994; Hooi, Tee & Lim, 2003; Fulkerson & Meek, 1998; Taylor, 2009; Morais, 2010; Lander & Auger, 2008). Bagi ciri kualitatif penyata kewangan membincangkan tentang materialiti (Maines & McDaniel, 2000; Mills, 1989), kebolehbacaan dan kefahaman (Power, 2003; Sun, 2007).

Selain itu, kajian juga membentangkan tentang ketekalan di dalam persembahan laporan tahunan, tempoh perakaunan dan perbandingan maklumat (Taylor, 2009; Smith & Smith, 1971; Neumann, 2000). Pembentangan penyata kewangan dibahagikan kepada bahasa (Mills, 1989; Parker, 1994; Benston, 1982; Hassan & Saleh, 2010; Geoff, 2004; Globerman, Peng & Shapiro, 2011; Hjarvard, 2003), penemuan daripada kajian lepas memaparkan tentang penerimaan IFRS (Tan, Jane & Othman, 2007), kepentingan format persembahan (Smith, 1971; Laswad, Ghani & Tooley, 2008), penyata untung rugi dan penyata pendapatan menyeluruh (Melis & Carta, 2010; Beattie, Brown & Ewers, 1994), kunci kira-kira, penyata perubahan ekuiti, penyata aliran tunai dan kerelevanan (Lander & Auger, 2008; Taylor, 2009; Kosmala, 2003; Lau Chee Kwong, 2008; Scott, 2006). Laporan tahunan yang dipaparkan perlulah mudah dibaca dan difahami. Sesuatu laporan tahunan perlu mempunyai tahap kebolehbacaan dan kefahaman yang tinggi supaya dapat memudahkan pengguna mendapatkan maklumat yang diperlukan. Walau bagaimanapun,



terdapat beberapa perubahan hasil dari semakan FRS 101 antaranya adalah perubahan tajuk bagi setiap komponen penyata kewangan dan perubahan terhadap komponen penyata kewangan. Perubahan ini bertujuan memastikan pembentangan penyata kewangan lebih relevan. Berdasarkan kajian yang telah dijalankan, beberapa isu perlu diberi perhatian adalah berkenaan dengan penggunaan terminologi, bahasa, piawaian, tajuk dan istilah yang digunakan dalam laporan tahunan syarikat di Malaysia perlu dikaji dengan lebih lanjut lagi.

METODOLOGI

Metodologi yang digunakan di dalam kajian ini membincangkan kaedah untuk mendapatkan data. Secara keseluruhannya, bahagian ini bertujuan bagi menjelaskan bagaimana data diperolehi dan bagaimana data yang diperlukan itu dianalisis. Aspek yang akan disentuh termasuklah populasi dan sampel, reka bentuk kajian, instrumen kajian, kaedah pengumpulan data dan juga cara data dianalisis. Populasi kajian ini adalah menerusi laporan tahunan bagi syarikat berhad yang disenaraikan di Bursa Malaysia. Bertepatan dengan objektif kajian, pengkaji membuat pemerhatian ke atas laporan tahunan selama dua belas tahun iaitu bermula dari tahun 2001 hingga 2012. Populasi kajian ini adalah terhadap laporan tahunan yang menggunakan terminologi dan istilah perakaunan dalam Bahasa Melayu ataupun dwi-bahasa yang disediakan oleh syarikat awam yang disenaraikan di Pasaran Utama Bursa Malaysia. Bilangan populasi pada tahun 2012 didapati bahawa terdapat sebanyak 809 buah syarikat yang terdiri daripada pelbagai latar belakang yang berbeza disenaraikan di Pasaran Utama Bursa Malaysia. Daripada jumlah ini, tinjauan awal kami mendapati sebanyak 263 buah syarikat sahaja pada tahun 2001 sehingga tahun 2012 yang menerbitkan laporan tahunan dalam dwi-bahasa iaitu Bahasa Melayu dan Bahasa Inggeris.

Tumpuan kajian hanya akan diberikan terhadap semua istilah dan terminologi perakaunan yang digunakan di dalam penyata kedudukan kewangan, penyata kewangan komprehensif, penyata aliran tunai dan juga penyata perubahan ekuiti, termasuk nota-nota kepada akaun sesuatu laporan tahunan yang disediakan dalam Bahasa Melayu. Reka bentuk dalam kajian ini digunakan untuk menstruktur proses penyelidikan serta menunjukkan setiap bahagian penting seperti sampel data, pengukuran dan penilaian dapat disatukan untuk membentuk sesuatu keputusan. Kajian ini menggunakan reka bentuk yang berasaskan tinjauan dalam pengumpulan sesuatu data. Kajian yang dijalankan ini merupakan penyelidikan dan tinjauan deskriptif untuk menilai dan melihat keadah pembentangan yang dilakukan oleh syarikat berasaskan piawaian pelaporan kewangan. Dalam kajian ini, penyelidik hanya memilih kaedah secara tinjauan ke atas laporan tahunan syarikat. Ia merupakan salah satu kaedah utama yang dapat digunakan untuk mengumpul maklumat agar memenuhi objektif kajian (Neumann, 2000). Teknik persampelan secara bertujuan digunakan dalam kajian ini bagi tujuan pemilihan sampel. Teknik ini diperolehi dengan mendapatkan data dan maklumat daripada laman sesawang sampel syarikat kajian yang terdapat di laman sesawang Bursa Malaysia.

Analisis kandungan turut digunakan untuk menganalisis pelaporan maklumat di dalam penyata kewangan tahunan seperti maklumat yang lebih terperinci tentang tajuk, item, istilah, dan isi kandungan yang penting di dalam penyata kewangan bagi tujuan kajian ini berdasarkan syarikat tersenarai di Bursa Malaysia. Instrumen kajian menggunakan senarai semakan untuk mengumpul data. Soalan yang direka adalah berstruktur di mana maklumat yang disediakan dipetik daripada Piawaian Pembentangan Kewangan (PPK) 101 terbitan MASB. Bentuk soalan yang dirangka adalah berbentuk *closed item* merupakan bentuk soalan yang memerlukan pengkaji menjawab soalan dengan menanda jawapan pilihan yang telah disediakan (Sekaran, 2003). Kaedah pengumpulan data digunakan untuk melihat sama ada istilah-istilah ini mengikut seperti yang dicadangkan FRS 101, ujian kekerapan digunakan di dalam kajian ini bagi mencapai objektif yang dinyatakan. Ujian ini akan menunjukkan bukti dalam menyatakan bahawa penggunaan sesuatu istilah dan terminologi itu seragam digunakan di dalam industri (Golafshani, 2003) Data yang berbentuk kuantitatif akan dianalisis menggunakan perisian *Statistical Package for the Social*

Science (SPSS) versi 17.0. Semasa proses penganalisis data, penyelidik menggunakan kaedah analisis kekerapan bagi mencari kekerapan ke atas data yang diperolehi. Di samping itu, penyelidik juga menggunakan kaedah peratusan bagi menilai keputusan kajian dengan lebih mudah difahami.

Seterusnya, senarai semakan merupakan salah satu kaedah kuantitatif yang digunakan bagi mengumpul maklumat daripada mereka yang berpengalaman. Weber (1990) menyatakan bahawa senarai semakan dapat meningkatkan kesahihan sesuatu fakta. Kajian ini menggunakan kaedah tinjauan senarai semakan kerana merupakan satu kaedah bagi mendapatkan maklumat daripada entiti yang lebih berpengalaman. Dalam konteks ini, entiti yang berpengalaman merujuk kepada akta dan piawaian yang digunakan sebagai panduan dalam penyediaan penyata kewangan. Dianggarkan lebih daripada 95% daripada soalan yang dirangka berpandukan kepada piawaian yang sedia ada bagi memenuhi objektif yang telah ditetapkan.

DAPATAN KAJIAN

Jadual 1 menunjukkan bilangan syarikat yang menggunakan Bahasa Melayu bagi laporan tahunan di dalam laman web syarikat. Kesemua sampel kajian ini iaitu 263 buah syarikat mewakili 100% menggunakan Bahasa Melayu dalam penyediaan laporan tahunan. Walau bagaimanapun, dapatan yang diperolehi mengikut jumlah keseluruhan senarai syarikat di Bursa Malaysia mendapati bahawa pada tahun 2001 sebanyak 4.19%, diikuti dengan 3.75% pada tahun 2002, 3.43% pada tahun 2003, seterusnya 3.11% pada tahun 2004, 2.84% pada tahun 2005, 1.78% pada tahun 2006 dan 1.62% sahaja pada tahun 2007. Dapatan kajian ini menunjukkan penurunan daripada tahun 2001 sehingga tahun 2007. Bermula pada tahun 2008, terdapat sedikit peningkatan iaitu sebanyak 2.34%, namun semakin berkurang menjelang tahun 2009 iaitu sebanyak 2.13% diikuti dengan 1.90% pada tahun 2010. Pada tahun 2011 terdapat sedikit penurunan iaitu sebanyak 1.46% sahaja manakala pada tahun 2012 jumlah peratusan semakin meningkat iaitu 2.10%. Hasil dapatan ini menyokong kajian yang dijalankan oleh Parker (2004) yang menunjukkan bahawa Bahasa Melayu kurang digunakan oleh syarikat di Malaysia kerana Bahasa Inggeris telah menjadi lingua franca yang digunakan bagi urusan perniagaan dan kini Bahasa Inggeris juga dijadikan bahasa perniagaan.

Jadual 2 menunjukkan penyenaian syarikat di Bursa Malaysia mengikut tahun. Hasil dapatan menunjukkan bermula pada tahun 2001 sehingga 2012 sebanyak 100% adalah daripada sampel syarikat disenaraikan di Pasaran Utama Bursa Malaysia. Jadual ini juga menunjukkan peratusan keseluruhan syarikat *Government Linked Companies (GLC)* iaitu syarikat yang terdiri daripada syarikat yang berada di bawah kawalan Kerajaan Negeri dan agensi peringkat Negeri masing-masing. Pada tahun 2001 sebanyak 15 iaitu 6% daripada syarikat tersenarai dalam GLC, sebanyak 12 mewakili 4.65% buah syarikat pula tersenarai pada tahun 2003. Walau bagaimanapun, pada tahun 2007 pula mewakili 2.35% iaitu lapan buah syarikat GLC yang menggunakan Bahasa Melayu dalam laporan tahunan. Tahun 2010 mencatatkan jumlah sebanyak 6 buah syarikat mewakili 1.71%, manakala pada tahun 2012 mencatatkan bilangan meningkat iaitu 1.73% sahaja berbanding pada tahun 2011 mencatatkan bilangan syarikat sebanyak 1.31% sahaja daripada keseluruhan syarikat.

Jadual 3 menunjukkan tajuk yang digunakan bagi penyata kedudukan kewangan. Pada tahun 2010, terdapat sebanyak sembilan syarikat iaitu 56.2% yang menggunakan tajuk penyata kedudukan kewangan manakala tiga iaitu 18.7% menggunakan tajuk kunci kira-kira dan dua iaitu 12.5% menggunakan tajuk penyata posisi kewangan dan juga lembaran imbalan. Seterusnya bagi tajuk kunci kira-kira, tahun yang paling tinggi adalah pada tahun 2004 iaitu sebanyak 20 mewakili 71.43% dan paling rendah adalah pada tahun 2010 iaitu sebanyak tiga mewakili 18.7%. Bagi lembaran imbalan pula tahun yang paling tinggi adalah pada tahun 2001 iaitu sebanyak 17 mewakili 50% dan paling rendah pada tahun 2010 iaitu sebanyak dua mewakili 12.5% sahaja. Ini menunjukkan bahawa syarikat mula memberikan tumpuan dan kesedaran terhadap tajuk yang digunakan oleh syarikat sampel kajian adalah penyata kedudukan kewangan dan penyata posisi kewangan bermula pada tahun 2010. Berdasarkan FRS 101, menyatakan



bahawa perubahan piawaian terhadap tajuk bagi kunci kira-kira kepada tajuk penyata kedudukan kewangan ataupun penyata posisi kewangan disediakan oleh syarikat berdasarkan sampel yang disenaraikan di Bursa Malaysia.



Bahasa Melayu	2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012	
	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%
Ya	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100
Tidak	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Jumlah	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100
Jumlah Keseluruhan	812	4.19	853	3.75	874	3.43	900	3.11	914	2.84	899	1.78	863	1.62	855	2.34	844	2.13	844	1.90	822	1.46	809	2.10

Jadual 1: Penggunaan Bahasa Melayu dalam Laporan Tahunan

Jadual 2: Penggunaan Bahasa Melayu dalam Laporan Tahunan Syarikat Disenaraikan

Syarikat Disenaraikan	2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012	
	<i>f</i>	%	<i>f</i>	%	<i>F</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%
Pasaran Utama	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100
Papan ACE	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Syarikat PN17	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Syarikat GN3	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Jumlah	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100
Jumlah Keseluruhan	812	4.19	853	3.75	874	3.43	900	3.11	914	2.84	899	1.78	863	1.62	855	2.34	844	2.13	844	1.90	822	1.46	809	2.10
Jumlah GLC	15	100	14	100	12	100	13	100	11	100	7	100	8	100	9	100	7	100	6	100	6	100	8	100
Jumlah Keseluruhan GLC	250	6.0	258	5.43	258	4.65	320	4.1	334	3.29	337	2.1	340	2.35	342	2.63	347	2.0	350	1.71	458	1.31	462	1.73

**Jadual 3: Tajuk Penyata Kedudukan Kewangan**

Tajuk	2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012	
	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%
Penyata posisi kewangan	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2	12.5	6	50	9	52.94
Penyata kedudukan kewangan	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	9	56.2	5	41.67	5	29.41
Kunci kira-kira	17	50.0	19	59.38	17	56.66	20	71.43	19	73.08	3	18.75	3	21.4	6	30	6	33.3	3	18.7	1	8.33	3	17.65
Lembaran imbangan	17	50.0	13	40.63	13	43.33	8	28.57	7	26.92	13	81.25	11	78.6	14	70	12	66.6	2	12.5	-	-	-	-
Jumlah	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100

Jadual 4 menunjukkan tajuk yang digunakan bagi penyata pendapatan. Pada tahun 2010, terdapat sebanyak 13 iaitu 81.2% yang menggunakan tajuk penyata pendapatan komprehensif manakala tiga iaitu 18.7% menggunakan tajuk penyata pendapatan. Selain itu, pada tahun 2001 hingga 2009 menggunakan tajuk penyata pendapatan sebanyak 100% iaitu keseluruhan syarikat. Ini bermakna pada tahun 2010 hingga 2012 sahaja terdapat perbezaan dari segi tajuk penyata pendapatan yang digunakan oleh syarikat. Pada tahun 2011 mencatatkan 33.33% menggunakan tajuk penyata pendapatan komprehensif dan 66.67% menggunakan tajuk penyata pendapatan. Manakala bagi tajuk akaun untung dan rugi, penyata untung dan rugi, penyata untung serta lain-lain tajuk tidak digunakan oleh syarikat. Menurut FRS 101, memperuntukkan bahawa tajuk penyata pendapatan komprehensif merupakan satu piawaian bagi syarikat yang tersenarai di Bursa Malaysia.

Jadual 5 menunjukkan terminologi dalam penyata aliran tunai yang dilaporkan di dalam penyata kewangan. Terminologi aliran tunai daripada aktiviti operasi pada tahun 2008 paling tinggi iaitu sebanyak 20 mewakili 100% diikuti dengan 18 iaitu 100% pada tahun 2009 dan paling rendah adalah pada tahun 2001 iaitu sebanyak 5 mewakili 14.7% sahaja. Manakala bagi terminologi aliran tunai daripada aktiviti pelaburan pula adalah paling tinggi pada tahun 2009 iaitu sebanyak 18 mewakili 100% diikuti dengan 17 mewakili 85% pada tahun 2008 dan pada tahun 2003 paling rendah iaitu 7 mewakili 23.33% sahaja. Aliran tunai daripada aktiviti kewangan adalah paling tinggi pada tahun sebanyak 16 iaitu 61.54% pada tahun 2005, seterusnya pada tahun 2003 sebanyak 10 mewakili 33.33% sahaja. Tunai dan persamaan tunai pula mencatatkan jumlah paling tinggi pada tahun 2008 iaitu sebanyak 20 mewakili 100% manakala paling rendah iaitu 7 mewakili 20.59% sahaja. Terminologi pelarasan paling tinggi pada tahun 2008 iaitu sebanyak 16 mewakili 80% manakala bilangan paling rendah iaitu sebanyak 3 mewakili 10.71% pada tahun 2004. Seterusnya terminologi pembiayaan paling tinggi pada tahun 2005 iaitu sebanyak 19 mewakili 73.08% dan paling rendah pada tahun 2002 iaitu sebanyak 6 mewakili 18.75%. Akhir sekali bagi terminologi perubahan modal kerja pula adalah paling tinggi pada tahun 2012 sebanyak 17 iaitu 100% diikuti dengan 10 iaitu 29.41% pada tahun 2001 dan paling rendah adalah pada tahun 2010 iaitu 4 mewakili 25% sahaja.

Jadual 6 menunjukkan kaedah aktiviti operasi yang digunakan. Bilangan syarikat yang paling tinggi menggunakan kaedah langsung adalah pada tahun 2004 iaitu sebanyak 8 mewakili 28.57% diikuti dengan 5 mewakili 14.71% pada tahun 2001 manakala yang paling rendah adalah pada tahun 2002 iaitu sebanyak 2 mewakili 6.25% sahaja. Kaedah langsung merupakan kaedah yang tidak memerlukan pelarasan di dalam penyata aliran tunai, manakala kaedah tidak langsung pula memaparkan pelarasan pada penyata aliran tunai. Seterusnya bagi syarikat yang menggunakan kaedah tidak langsung adalah paling tinggi pada tahun 2002 iaitu sebanyak 30 mewakili 93.75% diikuti dengan 29 mewakili 85.29% pada tahun 2001 manakala yang paling rendah adalah pada tahun 2010 iaitu 11 mewakili 68.7% sahaja.

Jadual 7 menunjukkan penyata yang dilaporkan dahulu di dalam penyata kewangan. Tahun yang paling tinggi melaporkan tajuk penyata kedudukan kewangan adalah pada tahun 2002 iaitu sebanyak 22 iaitu 68.75% manakala yang paling rendah adalah tahun 2009 iaitu sebanyak tiga mewakili 16.6%. Seterusnya, bagi tajuk penyata pendapatan komprehensif pula tahun paling tinggi adalah pada tahun 2001 iaitu 19 mewakili 55.88% manakala tahun paling rendah adalah pada tahun 2005 iaitu sebanyak tujuh mewakili 26.92% sahaja.

**Jadual 4:** Tajuk bagi Penyata Pendapatan Komprehensif

Tajuk	2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012	
	<i>F</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%
Penyata pendapatan komprehensif	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	13	81.2	4	33.33	6	35.29
Akaun untung dan rugi	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Penyata untung dan rugi	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	3	17.65	
Penyata pendapatan	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	3	18.7	8	66.67	8	47.06
Jumlah	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100

Jadual 5: Terminologi dalam Penyata Aliran Tunai

Terminologi	2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012	
	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>F</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%
Aliran tunai daripada aktiviti operasi	5	14.7	16	50.0	5	16.66	12	42.86	16	61.54	16	100	14	100	20	100	18	100	11	68.7	5	41.67	12	70.59
Aliran tunai daripada aktiviti pelaburan	11	32.35	10	31.25	7	23.33	9	32.14	12	46.15	15	93.75	14	100	17	85	18	100	7	43.7	7	58.33	9	52.94
Aliran tunai daripada aktiviti kewangan	10	29.41	12	37.5	10	33.33	8	28.57	16	61.54	3	18.75	2	14.3	8	40	6	33.3	7	43.7	10	83.33	8	47.06
Tunai dan persamaan tunai	7	20.59	11	34.38	11	36.66	11	39.29	11	42.31	15	93.75	11	78.6	20	100	18	100	16	100.0	11	91.67	11	64.71
Pelarasan	14	41.18	10	31.25	13	43.33	3	10.71	13	50.0	14	87.5	11	78.6	16	80	14	77.7	11	68.7	12	100	3	17.65
Pembiayaan	18	52.29	6	18.75	18	60.0	9	32.14	19	73.08	11	68.75	13	92.9	9	45	13	72.2	9	56.2	5	41.67	9	52.94
Perubahan modal kerja	10	29.41	9	28.3	17	56.66	17	60.71	6	23.08	-	-	-	-	7	35	6	33.3	4	25.0	8	66.67	17	100

**Jadual 6:** Kaedah Aktiviti Operasi yang Digunakan

Kaedah	2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012	
	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%
Kaedah langsung	5	14.71	2	6.25	2	6.66	8	28.57	3	11.54	2	12.5	3	21.4	4	20	4	22.2	5	31.2	5	41.67	4	23.53
Kaedah tidak langsung	29	85.29	30	93.75	28	93.33	20	71.43	23	88.46	14	87.5	11	78.6	16	80	14	77.7	11	68.7	7	58.33	13	76.47
Jumlah	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100

Jadual 7: Penyata yang Dilaporkan Dahulu

Penyata	2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012	
	<i>F</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%	<i>f</i>	%
Penyata kedudukan kewangan	15	44.12	22	68.75	14	46.66	20	71.43	19	73.08	3	18.75	4	28.6	10	50	3	16.6	4	25.0	5	41.67	7	41.18
Penyata pendapatan komprehensif	19	55.88	10	31.25	16	53.33	8	28.57	7	26.92	13	81.25	10	71.4	10	50	15	83.3	12	75.0	7	58.33	10	58.82
Jumlah	34	100	32	100	30	100	28	100	26	100	16	100	14	100	20	100	18	100	16	100	12	100	17	100

KESIMPULAN & PERBINCANGAN

Hasil kajian yang dijalankan adalah untuk mencapai objektif kajian iaitu untuk meneliti pelaporan dan pembentangan laporan kewangan berdasarkan FRS 101 ke atas syarikat tersenarai di Bursa Malaysia. Berdasarkan kajian, sampel syarikat mendapati penyata kewangan kumpulan dan syarikat disediakan selaras dengan peruntukan Akta Syarikat 1965 dan penggunaan FRS 101. Bahkan piawaian ini turut diterima pakai secara berperingkat oleh sampel syarikat. Kajian ini melaporkan dapatan kajian berkaitan amalan perakaunan di kalangan syarikat tersenarai di Bursa Malaysia berdasarkan garis panduan yang ditetapkan oleh MASB 1. Hasil kajian mendapati kadar penggunaan Bahasa Inggeris sebagai bahasa yang digunakan dalam laporan tahunan syarikat sangat tinggi (melebihi 95%). Hasil analisis juga mendapati bahawa majoriti syarikat di Malaysia membentangkan tajuk dalam penyata kewangan seperti kunci kira-kira, penyata pendapatan, penyata perubahan ekuiti, penyata aliran tunai dan pelaporan nota kepada penyata kewangan adalah seragam.

Berdasarkan perbezaan yang wujud dari segi susun atur, penggunaan terminologi dan istilah serta kaedah perakaunan yang digunakan, ia menggambarkan bahawa objektif piawaian FRS 101 untuk menetapkan asas pembentangan penyata kewangan tujuan umum bagi memastikan kebolehbandingan dengan penyata kewangan terdahulu perusahaan itu sendiri dengan penyata kewangan perusahaan lain, sukar dicapai. Penggunaan Bahasa Inggeris memang digalakkan oleh kerajaan, namun dari satu aspek lain iaitu sama ada maklumat yang disampaikan oleh syarikat melalui laporan tahunan mereka dapat difahami dengan baik oleh para pengguna yang tidak mahir berbahasa Inggeris menimbulkan satu persoalan lain (Lander & Auger, 2008). Oleh itu, adalah dicadangkan penggubal piawaian perakaunan untuk meneliti perkara ini sama ada perlu atau tidak untuk pihak syarikat menyediakan laporan tahunan syarikat mereka dalam sekurang-kurangnya dua bahasa agar kebolehgunaan dan kebolehfahamannya dipertingkatkan di kalangan pengguna. Berdasarkan perbezaan yang wujud dari segi susun atur, penggunaan terminologi dan istilah serta kaedah perakaunan yang digunakan, ia menggambarkan bahawa objektif piawaian MASB 1 untuk menetapkan asas pembentangan penyata kewangan tujuan umum bagi memastikan kebolehbandingan dengan penyata kewangan terdahulu perusahaan itu sendiri dengan penyata kewangan perusahaan lain, sukar dicapai (Jones, 1996). Bagi penggunaan FRS 101, kepentingan kumpulan dalam entiti dikawal bersama dimasukkan ke dalam penyata kewangan disatukan mengikut kaedah perakaunan entiti. Hasil analisis mendapati bahawa majoriti syarikat di Malaysia membentangkan tajuk dalam penyata kewangan bagi industri seperti kunci kira-kira, penyata pendapatan, penyata perubahan ekuiti, penyata aliran tunai dan pelaporan nota kepada penyata kewangan adalah seragam.

Kajian ini disokong oleh kajian Adelberg & Farrrelly (1989) yang melaporkan maklumat berikut mematuhi keperluan yang diperuntukkan oleh FRS 101. Namun begitu, seperti mana kajian Parker (1994) yang membincangkan tentang penggunaan istilah, bahasa dan terminologi secara diskriptif, masih terdapat perbezaan daripada beberapa aspek yang dikaji seperti terminologi, istilah dan kaedah yang dibentangkan dalam laporan tahunan syarikat. Walau bagaimanapun terdapat beberapa kekangan sewaktu kajian dijalankan, FRS 101 masih belum dipraktikkan oleh syarikat sepenuhnya kerana MFRS 101 akan digunakan sepenuhnya oleh setiap syarikat yang tersenarai di Bursa Malaysia bermula pada tahun 2012. Jumlah sampel yang dijadikan kajian adalah rendah dan terhad iaitu sebanyak 263 buah syarikat yang menggunakan terminologi dan istilah dalam Bahasa Melayu di dalam laporan tahunan yang tersenarai di Bursa Malaysia pada tahun 2001 sehingga tahun 2012. Kajian yang dijalankan hanya bertumpu kepada syarikat yang tersenarai di Pasaran Utama Bursa Malaysia. Oleh itu, dapatan kajian ini menggambarkan praktis pembentangan laporan tahunan di kalangan syarikat tersenarai di Pasaran Utama Bursa Malaysia sahaja. Seterusnya kajian ini dilaksanakan di persekitaran pelaporan tahunan berasaskan laman sesawang syarikat di Malaysia. Berdasarkan kajian yang telah dijalankan oleh penyelidik, kajian lanjutan perlu dijalankan kerana kajian kini hanya dibuat pada pra pelaksanaan MFRS 101.

Kajian pada masa hadapan boleh diperkembangkan lagi kepada penelitian kesan pembentangan MFRS 101 disemak semula bagi penyata kewangan dalam hal yang berkenaan terhadap entiti laporan tahunan dalam mengklasifikasikan maklumat perbandingan. Penyata kewangan juga menunjukkan keputusan pengawasan ke atas sumber yang diamanahkan kepadanya. Walau bagaimanapun terdapat

kemungkinan bahawa penyata kedudukan kewangan dan penyata pendapatan komprehensif akan dibentangkan sebagai piawaian prestasi (Feltham, Indjejikian & Nanda, 2006). Kajian seumpama ini akan menambahkan bukti sokongan tentang kesan peralihan sepenuhnya piawaian kepada MFRS 101 di dalam laporan kewangan mulai tahun 2012. Selain itu, cadangan yang boleh dipertimbangkan adalah mempertingkatkan populasi dan sampel kajian yang dijalankan. Jumlah sampel kajian yang mencukupi dan seimbang adalah penting bagi memperolehi data yang lebih tepat dan mewakili populasi sampel. Kajian ini juga boleh dijalankan dengan membuat perbandingan antara karakter spesifik syarikat dengan praktis penerimaan FRS 101.

Di samping itu, hasil kajian ini dapat menjadi satu alternatif kepada syarikat untuk meningkatkan tahap pengetahuan dalam pelaksanaan MFRS 101 di dalam penyediaan penyata kewangan, sejajar dengan langkah MASB untuk melaksanakan MFRS 101 mulai tahun 2012. Di samping itu, isu penggunaan bahasa dan pemahaman terhadap tajuk penyata kewangan perakaunan yang digunakan dalam laporan tahunan syarikat juga boleh diberi perhatian untuk kajian akan datang bagi menentukan sama ada penggunaan bahasa menghadkan kebolegunaan laporan tahunan syarikat di kalangan pengguna. Oleh yang demikian, dapat disimpulkan bahawa kajian ini memberikan bukti awal tentang penggunaan piawaian pelaporan kewangan pada peringkat pertama diperkenalkan, dilaksanakan secara menyeluruh dari segi amalan pembentangan penyata kewangan di kalangan syarikat berhad di Malaysia. Namun begitu, peringkat ini masih terlalu awal untuk melihat perkembangan sebenar penerimaan MFRS 101 bagi syarikat berhad di Malaysia sebagai peralihan sepenuhnya MFRS 101 mulai tahun 2012. Kajian yang dijalankan ini merupakan titik permulaan terhadap penggunaan istilah dan terminologi laporan tahunan dalam Bahasa Melayu.

Oleh itu, adalah dicadangkan penggubal piawaian perakaunan untuk meneliti perkara ini sama ada perlu atau tidak untuk pihak syarikat menyediakan laporan tahunan syarikat mereka dalam sekurang-kurangnya dua bahasa agar kebolegunaan dan kebolehfahamannya dipertingkatkan di kalangan pengguna. Selain itu, pihak syarikat juga perlulah mempunyai kesedaran dan keseragaman dalam melaporkan laporan tahunan mereka bagi memudahkan maklumat perakaunan disampaikan kepada pengguna dan juga pihak berkepentingan dengan lebih berkesan. Pihak syarikat di Malaysia perlu mengambil inisiatif dan mematuhi piawaian yang telah ditetapkan oleh FRS 101 bagi mengelakkan daripada kekeliruan maklumat yang ingin disampaikan. Kajian pada masa akan datang juga diharapkan dapat menjelaskan tentang respon penyedia laporan tahunan terhadap sebab dan faktor penggunaan istilah dan terminologi yang berbeza. Selain itu, kajian berikutnya dapat memberikan tumpuan terhadap indeks laporan tahunan di dalam Bahasa Melayu. Akhir sekali, diharap kajian ini dan kajian berterusan dalam amalan perakaunan diharap dapat memberi sumbangan dan input yang berguna kepada penggubal dasar, pihak yang terbabit dan pihak yang berkepentingan dalam bidang perakaunan untuk menambah baik amalan perakaunan di Malaysia.

PENGHARGAAN

Geran penyelidikan diperoleh daripada Kementerian Pelajaran Malaysia (KPM) dan Pusat Pengurusan Penyelidikan (RMC), Universiti Teknologi Malaysia, Johor Bahru, Johor Darul Ta'zim di bawah skim Geran Universiti Penyelidikan (GUP) Tier 1 Q.J130000.2529.09H11 amat dihargai. Penulis ingin merakamkan jutaan terima kasih kepada Norhayati Salleh dan Shatira Mohd Zaini dalam menyempurnakan manuskrip penyelidikan ini.

RUJUKAN

- Adelberg, A.H., & Farrelly, G.E. (1989). Measuring the Meaning of Financial Statement Terminology: A Psycholinguistics Approach. *Journal of Accounting and Finance*, 127(6), 33-40.
- Aisbitt, S., & Nobes, C. (2001). The True and Fair View Requirement in Recent National Implementation. *Accounting and Business Research*, 31(2), 83-90.
- Alexander, D. (1993). A European true and fair view. *European Accounting Review*. 2(1), 59-80.

- Ali, A., Chen, T., & Radhakrishnan, S. (2007). Corporate disclosures by family Firms. *Journal of Accounting and Economics*, 44(12), 238-286.
- Ali Khan, M.N.A. & Mohd Zaini, S. (2012). Amalan Penggunaan Bahasa Melayu dalam Laporan Tahunan Syarikat di Malaysia. *Jurnal Teknologi*, 59, 125-134.
- Archer, S., & McLeay, S. (1991). Issues in transnational financial reporting: A linguistic analysis. *Journal of Multi-Lingual and Multicultural Development*, 12(5), 61-347.
- Ashbaugh, H., & Pincus, M. (2001). Domestic accounting standards, international accounting standards, and the predictability of earnings. *Journal of Accounting Research*, 39(3), 34-417.
- Awang Sariyan. (1995). *Ceritera Bahasa*, Kuala Lumpur: Dewan Bahasa dan Pustaka.
- Awang Sariyan. (2000). *Warna dan Suasana Perancangan Bahasa Melayu di Malaysia*, Kuala Lumpur: Dewan Bahasa dan Pustaka.
- Baldwin, A.A., Dull, R.B., & Graham, A.W. (2003). Web-based Financial Statements: Hyperlink to Footnotes and their Effect on Decision. *International Journal of Accounting Information System*, 4(2), 185-203.
- Ball, R., Robin, A., & Wu, J. (2003). Incentives versus standards: Properties of accounting income in four East Asian countries. *Journal of Accounting and Economics*, 36(1), 70-235.
- Barker, R.G. (1998). The market for information: Evidence from finance directors, analysts and fund managers. *Accounting and Business Research*, 29(1), 3-20.
- Barth, M.E. (2008). Global financial reporting: implications for US academics. *The Accounting Review*, 83(15), 1159-1179.
- Barth, M., Landsman, W., & Lang, M. (2007). International accounting standards and accounting quality. *Journal of Accounting Research*, 46(3), 98-467.
- Bartov, E., Goldberg, S.R., & Kim, M. (2005). Comparative value relevance among German, US, and international accounting standards: A German stock market perspective. *Journal of Accounting, Auditing and Finance*, 20(2), 95-119.
- Beattie, V., Brown, S., Ewers, D., John, B., Manson, S., Thomas, D., & Turner, M. (1994). Extraordinary item and income smoothing: a positive accounting approach. *Journal of a Business Finance and Accounting*, 21(6), 811-848.
- Belkaoui, A.R., & Picur, R.D. (1991). Cultural determinism and the perception of accounting concepts. *The International Journal of Accounting*, 26(2), 30-118.
- Benston, G.J. (1982). Accounting and Corporate Accountability, Organizations and Society. *The International Journal of Accounting*, 7(2), 87-105.
- Beretta, S., & Bozzolan, S. (2004). A framework for the analysis of firm risk communication. *The International Journal of Accounting*, 21(6), 811-991.
- Booth, P. & Schulz A.K. (1995). The Effects of Presentation Format on The Effectiveness and Efficiency of Auditor's Analytical Review Judgements. *Journal of Accounting and Finance*, 12(3), 107-137.
- Botoson, C. (2004). Discussion of a Framework for the Analysis of Risk Communication. *The International Journal of Accounting*, 39, 289-295.
- Bradshaw, M., Bushee, B., & Miller, G. (2004). Accounting choice, home bias, and US investment in non-US firms. *Journal of Accounting Research*, 42(5), 795-841.
- Brennan, N., Guillaumon-Saorin, E., & Pierce, A. (2009). Impression Management: Developing and Illustrating a Scheme of Analysis for Narrative Disclosures: A Methodological Note. *Accounting, Auditing & Accountability Journal*, 22(5), 789-832.
- Brown, C. (1995). *Translation and Law: American Translators Association Scholarly Monograph Series*. Riding the Waves of Fortune: Translating Legislation of the Successor Soviet Republics, in Morris. (6th ed.) Amsterdam/Philadelphia: John Benjamins Publishing Company.
- Bursa Malaysia. 2010. Main market listing. Retrieved August 17, 2011, from <http://www.bursamalaysia.com/website/bm/regulation/rules/listing/>
- Carter, R., & Van Auken, H. (2006). Small Firm Bankruptcy. *Journal of Small Business Management*, 44(4), 493-512.
- Chan, K.C., & Seow, G.S. (1996). The association between stock return and foreign GAAP earnings versus earnings adjusted to US GAAP. *Journal of Accounting Research*, 96(2), 83-116.

- Chen, L.H., & Sami, H. (2008). Trading volume reaction to the earnings reconciliation from IAS to US GAAP. *Contemporary Accounting Research*, 25(1), 15-53.
- Courtis, John K. (1995). Readability of Annual Reports: Western versus Asian Evidence. *Accounting, Auditing and Accountability Journal*, 8(2), 4-17.
- Courtis, John K. (1998). Annual Report Readability Variability: Test of the Obfuscation Hypothesis. *Accounting, Auditing and Accountability Journal*, 11(4), 34-57.
- Covrig, V.M., DeFond, M.L., & Hung, M. (2007). Home bias, foreign mutual fund holdings, and the voluntary adoption of international accounting standards. *Journal of Accounting Research*, 45(1), 41-70.
- Craven, B.M., & Marston, C.L. (1997). Investor relations and corporate governance in large UK companies. *Corporate Governance*, 5(3), 51-137.
- Cuijpers, R., & Buijink, W. (2005). Voluntary adoption of non-local GAAP in the European Union: A study of determinants and consequences. *European Accounting Review*, 14(3), 487-524.
- Daske, H., Hail, L., Leuz, C., & Verdi, R. (2008). Mandatory IFRS Reporting Around the World: Early Evidence on the Economic Consequences. *Journal of Accounting Research*, 46, 1085-1142.
- Davidson, R.A., & Chrisman, H.H. (1993). Interlinguistic comparison of international accounting standards: The case of uncertainty expressions. *International Journal of Accounting*, 28(1), 1-16.
- Epstein, Barry J., & Eva K.J. (2008). Global Financial Reporting. The growing Prominence of IFRS: Implication for Transactional Attorneys. *Business Law International*, 9(1), 16-27.
- Evans, L. (2004). Language, Translation and the Problem of International Accounting Communication. *Accounting, Auditing and Accountability Journal*, 17(2), 210-248.
- Feltham, G., Indjejikian, R., & Nanda, D. (2006). Dynamic Incentives and Dual-Purpose Accounting. *Journal of Accounting and Economics*, 42, 37-417.
- Fulkerson, C.L., & Meek, G.K. (1998). Analysts' earnings forecast and the value relevance of 20F reconciliations from non-US GAAP. *Journal of International Financial Management and Accounting*, 9(1), 1-15.
- Geoff, M. (2004). Principle and Practices. *Journal of Accounting and Economics*, Retrieved Okt 9, 2010 from <http://www.oup.com.uk>
- Gerard, S. (2011). Let's Talk: Adapting Accountants' Communications to Small Business Managers Objectives and Preferences. *Accounting, Auditing & Accountability Journal*, 24(6), 781-809.
- Globerman, S., Peng, M.W., & Shapiro, D.M. (2011). Corporate governance and Asian companies. *Asia Pacific Journal of Management*, 28(2), 1-14.
- Golafshani, N. (2003). Understanding Reliability and Validity in Qualitative Research. *The Qualitative Report*, 8(4), 597-607.
- Hassan, M.S., & Mohd Salleh, N. (2010). The Value Relevance of Financial Instruments Disclosure in Malaysia Firms Listed in the Main Board of Bursa Malaysia. *International Journal of Economics and Management*, 4(2), 243-270.
- Healy, M., & Perry, C. (2000). Comprehensive Criteria to Judge Validity and Reliability of Qualitative Research within the Realism Paradigm. *Qualitative Market Research*, 3(3), 118-126.
- Hein, N., Beuren, I.M., & Klann, R.C. (2008). Impact of the IFRS and US-GAAP on economic-financial indicators. *Journal Managerial Auditing*, 23(7), 632-649.
- Hirst, D., & Hopkins, P. (1998). Comprehensive Income Reporting and Analysts' Valuation Judgement. *Journal of Accounting Research*, 36, 47-75.
- Hjarvard, S. (2003). The Globalization of Language: How the media contribute to the spread to English and the emergency of medialects. *Media, Globalization and Identity*, 23, 14-78.
- Holthausen, R., & Watts, R. (2001). The Relevance of the Value-Relevance Literature for Financial Accounting Standard Setting. *Journal of Accounting and Economics*, 31(1-3), 3-75.
- Hooi, L.W., Tee, K.W., & Lim, Y.K. (2003). *Fokus Ungu Masteri: SPM Prinsip Perakaunan*. Kuala Lumpur: Pelangi.
- Hopkins, P.E. (1996). The effect of financial statement classification of Hybrid financial instrumentation on financial analysts' stock price judgments. *Journal of Accounting Research*, 34, 33-50.

- IASC. (1999). *IASC Publisher Study of Business Reporting on the Internet*. Press Release: International Accounting Standards Committee, 15 November 1999.
- Iselin, E.R. (1989). The Effects of Format on the Extraction of Information From Accounting Statement. *Journal of Accounting and Finance*, 32, 73-79.
- Jeanjean, T., & Stolowy, H. (2008). Do accounting standards matter: An exploratory analysis of earnings management before and after IFRS adoption. *Journal of Accounting and Public Policy*, 27(6), 480-494.
- Jones, M.J. (1996). Readability of annual reports: Western versus Asian evidence. Comment to contextualize. *Accounting, Auditing and Accountability Journal*, 9(2), 4-17.
- Kosmala, M.K. (2003). The true and fair view construct in the context of the Polish transition economy: some local insights. *European Accounting Review*, 12(3), 87-465.
- Lander, G.L. & Auger, A.K. (2008). The need for transparency in financial reporting Implications of off-balance-sheet financing and inferences for the future. *Journal of Accounting & Organizational Change*, 4(1), 27-46.
- Laswad, F., Ghani, E.K., & Tooley, S. (2008). Do Digital Reporting Formats Assist Professional Users in Overcoming Functional Fixation in Recognition vs. Disclosure. *BAA 2008 Conference*. 15-19 April. Blackpool, 331-348.
- Lau Chee Kwong (2008). *Financial Reporting of Intangible Assets: The Realibility of Measurement Methods*. Doctor Philosophy, Universiti Putra Malaysia,
- Maines, L.A., & McDaniel, L.S. (2000). Effects of comprehensive income characteristics on nonprofessional investor's judgments: The role of financial statement presentation format. *The Accounting Review*, 75(2), 179-207.
- Melis, A., & Carta, S. (2010). Does accounting regulation enhance corporate governance: Evidence from the disclosure of share-based remuneration. *Journal of Management and Governance*, 14, 435-446.
- Mills, P.A. (1989). Words and the study of accounting history. *Accounting, Auditing, and Accountability Journal*, 2(1), 34-78.
- Mohd Iskandar, T., & Basnan, N. (2002). *Perakaunan Kewangan Prinsip dan Amalan di Malaysia*. (2nd ed.) Kuala Lumpur: Cerdik Publication.
- Morais, A. (2010). Actuarial gains and losses: the determinants of the accounting method. *Pacific Accounting Review*, 22 (1), 42-56.
- Neumann, F.L. (2000). Auditor reporting decisions. *Journal of Accounting & Economics*, 12(1), 78-114.
- Okada. H. (2008). The assets and liability view and the income concepts in Japan. *Malaysian Accounting Review*, 7(1), 87-115.
- Parker, R.H. (1994). Finding English words to talk about accounting concepts. *Accounting, Auditing and Accountability Journal*, 7(2), 47-82.
- Peng, S., & Bewley, K. (2010). Adaptability to fair value accounting in an emerging economy: A case study of China's IFRS convergence. *Accounting, Auditing & Accountability Journal*, 28(8), 982-1011.
- Porter, G.A., & Norton, C.L. (2010). Financial Accounting: The impact on decision makers. *South Western Cergage Learning*, 7, 62-64.
- Power, M. (2003). Auditing and the Production of Legitimacy. *Accounting, Organizations and Society*, 28, 379-394.
- Richardson, S.A., Tuna, A.I., & Wu, M. (2002). Predicting Earnings Management. *The Case of Earnings Restatements*, Retrieved August 3, 2011, from <http://ssrn.com/>
- Sekaran, U. (2003). *Research Methods For Business A Skill Building Approach* (4th ed.). USA: John Wiley & Sons, Inc.
- Scott, W.R. (1997). *Financial Accounting Theory*. London: Prentice-Hall
- Scott, W.R. (2006). *Financial Accounting Theory*. Toronto: Pearson Prentice-Hall.
- Smith, J., & Smith, N. (1971). Readability: A Measure of the Performance of The Communication Function of Financial Reporting. *Accounting Review*, 13, 352-361.

- Sun, M. (2007). An Exploratory Study of the Understandability of Listed Companies' Annual Reports. *Frontiers of Business Research in China*, 1(1), 39-49.
- Tan, L.L., Jane L., & Othman, R. (2007). *Adoption of Financial Reporting Standards (FRSs): Impact on Malaysia Companies*. Doctor Philosophy, Universiti Teknologi MARA, Shah Alam.
- Taylor, D.W. (2009). Costs-benefits of adoption of IFRSs in countries with different harmonization histories. *Asian Review of Accounting*, 17(1), 40-58.
- Thompson, J.C. (2008). When accounting finally becomes global. *The CP Accounting Journal*, 78(9), 115-241.
- Van Hulle, K. (1993). Truth and untruth about true and fair: A commentary on European true and fair view. *The European Accounting Review*, 2(1), 99-104.
- Weber, R.P. (1990). *Basic Content Analysis*. (2nd ed.). Newbury Park, CA: Sage.
- Yen, A., Hirst, D.E., & Hopkins, P. (2007). A Content Analysis of the Comprehensive Income Exposure Draft Comment Letters. *Research in Accounting Regulation*, 19, 53-79.
- Young, J. (2003). Constructing, Persuading and Silencing: The Rhetoric of Accounting Standards. *Accounting, Organizations and Society*, 28, 621-638.

Jabatan Perakaunan dan Kewangan
Fakulti Pengurusan
Universiti Teknologi Malaysia
81310 UTM Johor Bahru, Johor
MALAYSIA

Internet Financial Reporting of Malaysian Companies - A Study of Preparers' Perception

MOHD NOOR AZLI ALI KHAN
 Department of Accounting and Finance
 Faculty of Management
 Universiti Teknologi Malaysia
 81310 UTM Johor Bahru, Johor
 MALAYSIA
 m-nazli@utm.my

Abstract

This research analyses the issues of the current level of internet financial reporting (IFR) of the companies listed in Bursa Malaysia. According to a comprehensive review, the evaluation of IFR will be separated into two dimensions which are content dimension and presentation dimension. The items of disclosure in the dimensions of IFR disclosure index are based on the preparers' perception. Based on the research findings, the level of IFR started from 55.48 to 85.16 per cent. The findings also showed that the overall level of IFR listed companies in Bursa Malaysia were considered good. There is a slight increment from the previous similar study conducted. The implications of the research findings and future research have been discussed.

Key Words: content, presentation, preparers, internet financial reporting (IFR), Malaysia

INTRODUCTION

The growth of internet technology has increased the number of companies to disseminate their corporate information through website. The internet provides companies chances to supplement, replace and enhance traditional approach of stakeholders and investors communication (Marston & Polei, 2004). Besides, most of the companies prefer to use websites as a medium to disclose their information because it is cost effective, dynamic and flexible in worldwide. Now, companies' websites act as an important medium for corporate reporting (Trabelsi, Labelle & Laurin, 2004). For instance, websites have been utilized to deliver corporate information to investors and stakeholders (Abdelsalam & Street, 2007; Aly, Simon & Hussainey, 2010). In addition, through websites, companies can promote corporate identity (Poon, Li & Yu, 2003; Topalian, 2003) and deliver the information regarding organization and its activities (Chan & Wickramasinghe, 2006; Sriram & Laksamana, 2006).

Prior researches have shown that many of the companies in the global world have published and disclosed their corporate information via internet (Lymer, Debreceeny, Gray & Rahman, 1999; FASB, 2000; Oyelere, Laswad & Fisher, 2003; Marston & Polei, 2004). In most western countries, internet financial reporting (IFR) has become the norm for companies rather than exception (Gowthorpe, 2004). Therefore, in the context of accounting, website is an alternative platform which is vital for corporate information dissemination that includes annual report (Khan, 2006; Chan & Wickramasinghe, 2006; Sriram & Laksamana, 2006). Most of the researches regarding IFR in Malaysia are in descriptive form which covers issues like types of information reported (Ismail & Tayib, 2000), classification of web establishment on financial disclosure (Keliwon & Aziz, 2005), different IFR practices between Malaysia and Singapore (Khadaroo, 2005), information on the relationship with investors (Abdul-Hamid, 2005), the importance of Internet usage for Malaysia and Singapore investors (Abdul-Hamid et al., 2006), previous websites' content and graphic applications (Mohamad et al., 2006) and level of disclosure (Ali Khan & Ismail, 2011). Besides, there are a few explanatory studies took place such as determinant factors that influence IFR (Hassan et al., 1999;

Abdul-Hamid & Salleh, 2005; Hanifa & Ab. Rashid, 2005; Ali Khan, 2010; Ali Khan & Ismail, 2014) and determinant factors for Bursa Malaysia listed companies' financial reporting and internet environment (Al-Arussi et al., 2009).

FASB (2000) has identified the two dimensions of financial and business reporting which are content and presentation of information disclosed by companies' websites. Therefore, a comprehensive checklist with content dimension and presentation dimension is used to evaluate the current status of IFR based on preparers' perception in this research. Even though much research has been conducted in relation to IFR, there are still enquiries that need to be addressed, especially in the context of Malaysia. Among the enquiries, is the question concerning Malaysia's current IFR status quo. Therefore, the objective of this paper is to gather empirical evidence on the current status on the level of IFR among listed companies in Bursa Malaysia based on preparers' perception. This is due to the growth of information technology creates revolution in obtaining information beyond the world boundaries (Shiri, Salehi & Bigmoradi, 2013) and the dynamic nature of IFR (Uyar, 2012).

This paper is organized as follows. The next section provides the prior research in this study. The research methodology will be developed in the next section and followed by the findings and discussions. Lastly, conclusions are drawn at the end of this paper.

LITERATURE REVIEW

Since 1995, interest in the Internet has grown due to the availability of the World Wide Web (Jain & Kumar, 2013). A comprehensive review of existing literature on IFR shows a significant evolution of IFR research (Ali Khan & Ismail, 2012). The evolution of IFR research can be categorized into four themes; classification of IFR, descriptive studies, association studies and dimension of IFR (Ali Khan & Ismail, 2010). The research on IFR can be divided into three main categories: descriptive research by one or more countries, research by professional bodies and explanatory research (Ali Khan, 2010). Research related with IFR can be classified in the following three categories: research related to practical application of IFR in individual countries, research related to comparison of IFR practices between different countries and research into factors that affect IFR in individual countries (Bartulovic & Pervan, 2014).

Ali Khan and Ismail (2012) investigate the items which are important in IFR from the view of annual report preparers. The study employs the survey questionnaires in gathering information from the respondents on significant items that should be listed under IFR checklist. The result has shown five most important items in the current year which are: income statement of current year, balance sheet of current year, cash flow statement of current year, auditor report of current year, and annual report of current year (full text) which could illustrate the current content dimension. Presentation dimension on the other hand covers other five most important items which are the length of time taken to download the company's website, PDF annual report format, hyperlink to financial analysis, the existence of hyperlink in the annual report and link to the website. The result empirically proves that 87 items could be used for IFR checklist to ascertain IFR's level of disclosure.

The review of early previous studies provides an overview to the present research on the preparer's perception toward IFR. Purba et al. (2013) analyze the disclosure of financial statements in the company's state-owned enterprise in particular nature-based sector and manufacturing industries using IFR index, and analyze whether there is a relationship between the index of contents, index timeliness, technology index, the index of user support, the number of pages in and the wealth of the company's website. Jain and Kumar (2013) investigate stakeholders and user's perception towards the corporate financial reporting on internet of companies. The finding shows that responses were indicated that the requirement of financial reporting is in gaining significance among investors but still there are a number of investors who still prefer traditional format of reporting company performance.

Ali Khan and Ismail (2013) provide empirical evidence on the perception of Malaysian preparers and users of corporate annual reports about selected aspects of IFR. The perception of preparers and users of corporate annual reports were solicited using a survey mailed questionnaire. The findings of this

study suggested three main benefits to companies that engage in IFR are attract foreign investors, promote company wider to the public, and provide wider coverage. The findings also revealed that three main benefits to the users who collect financial information of companies via their website are increases timeliness and efficiency in obtaining financial information, makes investment decision process easier and faster, and provides information for company inexpensively.

Ali Khan and Ismail (2014) investigate empirically factors influencing Malaysian companies to disseminate their financial reports through Internet. This study examines relationship between level of IFR between contingency factor and firm specific characteristic of the company. IFR represented by two main dimensions which are dimension of content and presentation. Two factors for contingency factor and ten firm specific characteristics were identified. Specific characters of this study are measured using the three main variables: the structure, performance and market. Data were collected from 182 companies listed on the main board of Bursa Malaysia for the purpose of multiple regression analysis. The results showed that the three main features of the size of the company, the age of the company and return on equity significantly affect the level of IFR. The study also showed a negative relationship between profitability ratios with dimensions of contents and IFR overall index.

Bartulovic and Pervan (2014) find that there are differences in at the level of the IFR between observed countries. Ilias et al. (2014) investigate the response of expert users' towards IFR in Malaysia by focusing on perceived usefulness (PU), perceived ease of use (PEOU), perceived information quality (IQ), attitude, users' satisfaction and intention to re-use. The finding shows that PEOU, PU and IQ have a strong relationship with attitude, satisfaction and intention to re-use the IFGR in the decision-making process.

This study seeks to add to the existing literature on IFR in Malaysia. It does so by developing an index to measure the current status quo of IFR disclosure of voluntary financial and non-financial information on companies' websites in Malaysia.

METHODOLOGY

Sample and Data

The population of this research comprises of all public listed companies in Bursa Malaysia. However, in order to conduct this research, companies which listed under the financial industry, real estate investment trust and closed-end funds are not included in this research. This is because the financial industry is under the Malaysian banking institution besides subject to several rules and regulations of the Banking Institution Act 1998 outlined by the Bank Negara Malaysia (Rahmat & Mohd Iskandar, 2004; Abd Aziz, Mohd Iskandar & Mohd Saleh, 2006). Therefore, due to the different rules and regulations fall under the financial industry, real estate investment trust and closed-end funds, they have been excluded in this research (Ku Ismail & Chandler, 2004; Mohd Isa, 2006; Hashim & Mohd Saleh, 2007; Bue, Hassan & Md Nor, 2008). The complete list of 911 Bursa Malaysia 2013 listed companies as at 4th August 2014 (802 Main Market and 109 ACE Market) was obtained from Bursa Malaysia website.

According to Krejcie and Morgan (1970), the increasing demand for research has created a need for an efficient approach of determining the sample size needed to be representative of a given population. Therefore, a formula has been constructed in order to obtain the sample size needed. As a result, the sample size of this research based on the population of 802 companies is 280 companies (Krejcie and Morgan, 1970). The data have been collected during the January and February 2014. The IFR Index was measured by using a checklist which contain of two main sections namely, the content dimension and presentation dimension based on preparers' perception.

Measuring the Level of IFR

In order to measure the level of IFR, a checklist with a dichotomous answer (yes/no) where a score of 0 is given for no index and a score of 1 is given if there is an index. This checklist is used to evaluate the items presented in content and presentation dimension of a company's website. In the content

dimension, items are identified according to the information presented in the company's website. However, in the presentation dimension, items are evaluated based on the how the information is displayed (e.g. whether information is in the processable format) and how it facilitates to use (e.g. the existence of surfing engine). For each company, the level of IFR is measured through total score, which is counted as the total percentage of the ratio for the real score compared to the maximum score. In the context of preparer, the maximum score of IFR level is 155 points which content dimension contributed 97 points while presentation dimension contributed 58 points (details see Ali Khan, 2010; Ali Khan & Ismail, 2011; Ali Khan & Ismail, 2012). The score for the disclosure index was counted based on the exact total of the items reported compared to the total of maximum index items (Hossain et al., 1994; Naser, 1998; Camfferman & Cooke, 2002; Haniffa & Cooke, 2002; Naser, Al-Khatib & Karbhari, 2002; Bonson & Escobar, 2006; Hashim & Jaafar, 2006; Mohd Ghazali & Weetman, 2006; Abdelsalam et al., 2007; Curuk, 2008; Kelton & Yang, 2008; Al Arussi et al., 2009; Aly et al., 2010; Ali Khan, 2010; Ali Khan & Ismail, 2012). The formula as followed is used to calculate the IFR index.

$$\text{IFR index} = \frac{\text{Total real score obtained in content and presentation dimension}}{\text{Total maximum score}}$$

Findings and Discussions

Table 1 shows the profile of sample companies. Among the 280 of companies, there 31.07% of companies from industrial products, 23.93% from trading services, 17.86% from consumer products, 10.36% from properties, 5.36% from plantations, 5% from construction and technology. Lastly 0.36% from infrastructure project companies, hotels, mining and special acquisition company respectively.

TABLE 1: Profile of the Company

Sector of Industry	Number of Company	Percentage (%)
Industrial products	87	31.07
Trading services	67	23.93
Consumer products	50	17.86
Properties	29	10.36
Plantations	15	5.36
Construction	14	5.00
Technology	14	5.00
Infrastructure project companies	1	0.36
Hotel	1	0.36
Mining	1	0.36
Special purpose acquisition company	1	0.36
Total	280	100

Table 2 shows over the sample of 280 companies, 86.64% of the companies used pdf as the format of annual report. Besides, 14.64% of companies applied both pdf and html as the format of annual report. Lastly, only 0.72% of companies used pdf and flash as the format of annual report in their website.

TABLE 2: Format of Annual Report

Format	Number of Company	Percentage (%)
Pdf	237	84.64
Pdf and html	41	14.64
Pdf and flash	2	0.72
Total	280	100

Table 3 shows the type of information disclosed in the companies' website. The total of 280 sample companies has fully disclosed comprehensive financial statement and mostly more than five years they have disclosed. However, for important statement, around 74.29% of companies have disclosed and mostly more than five years.

TABLE 3: Type of information disclosed

Type of Information	Total		Number of years				
	No.	%	1	2	3	4	> 5
Comprehensive financial statement	280	100.00	13	12	13	10	252
Important statements	208	74.29	4	7	0	2	195

Table 4 shows the frequency of IFR reporting level of the 280 of sample companies. From the findings, the range of the disclosure index from 55.48 per cent (86 items) to 85.16 per cent (132 items). Two companies (0.71% of the sample companies) obtained the highest IFR which are Boustead Heavy Industries Corporation Berhad and Faber Group Berhad. On the other hands, there is one company (0.36 % of the sample companies) obtained the lowest IFR which is Kejuteraan Samudara Timur Berhad. Overall, the highest frequency of disclosure index falls on 65.81 per cent (102 items) with 17 of sample companies. According to Wallace (1988), company that attained an index disclosure of over 50 per cent was considered as having a good index disclosure. Therefore, it can be summarized that all the 280 of sample companies are considered of having a good satisfactory level of disclosure index.

TABLE 4: Level of Internet Financial Reporting (Overall)

Disclosure Index	No. of Item	Frequency	Percentage (%)
55.48	86	1	0.36
58.06	90	1	0.36
58.71	91	2	0.71
59.35	92	2	0.71
60.00	93	4	1.43
60.65	94	2	0.71
61.29	95	4	1.43
61.94	96	9	3.21
62.58	97	10	3.57
63.23	98	7	2.50
63.87	99	6	2.14
64.52	100	9	3.21
65.16	101	13	4.64
65.81	102	17	6.07
66.45	103	13	4.64
67.10	104	16	5.71
67.74	105	13	4.64
68.39	106	16	5.71
69.03	107	9	3.21
69.68	108	4	1.43
70.32	109	8	2.86
70.97	110	13	4.64
71.61	111	6	2.14
72.26	112	4	1.43
72.90	113	1	0.36
73.55	114	4	1.43
74.19	115	8	2.86
74.84	116	9	3.21
75.48	117	5	1.79
76.13	118	3	1.07
76.77	119	5	1.79
77.42	120	5	1.79
78.06	121	7	2.50
78.71	122	8	2.86
79.35	123	5	1.79
80.00	124	5	1.79

80.65	125	9	3.21
81.29	126	3	1.07
81.94	127	2	0.71
82.58	128	5	1.79
83.23	129	2	0.71
83.87	130	2	0.71
84.52	131	1	0.36
85.16	132	2	0.71
Total	155	280	100.00

Table 5 shows the level of IFR of content dimension index. From the findings, the range of the level of IFR in the context of content dimension is from 58.76 per cent (57 items) to 93.81 per cent (91 items). Based on the table, there is one company (0.36% of the sample) namely Kejuruteraan Samudara Timur Berhad which obtained the lowest IFR content dimension. There is only one company (0.36% of the sample) namely Euro Holdings Berhad which obtained the highest IFR content dimension. Overall, the highest frequency for index disclosure is 72 items (74.23 per cent).

TABLE 5: Level of Internet Financial Reporting for Content Dimension

Disclosure Index	No. of Item	Frequency	Percentage (%)
58.76	57	1	0.36
62.89	61	1	0.36
64.95	63	2	0.71
65.98	64	5	1.79
67.01	65	6	2.14
68.04	66	4	1.43
69.07	67	6	2.14
70.10	68	7	2.50
71.13	69	15	5.36
72.16	70	22	7.86
73.20	71	19	6.79
74.23	72	22	7.86
75.26	73	17	6.07
76.29	74	18	6.43
77.32	75	10	3.57
78.35	76	9	3.21
79.38	77	8	2.86
80.41	78	11	3.93
81.44	79	10	3.57
82.47	80	5	1.79
83.51	81	4	1.43
84.54	82	6	2.14
85.57	83	9	3.21
86.60	84	7	2.50
87.63	85	15	5.36
88.66	86	15	5.36
89.69	87	7	2.50
90.72	88	6	2.14
91.75	89	6	2.14
92.78	90	6	2.14
93.81	91	1	0.36
Total	97	280	100.00

Table 6 shows the level of IFR of presentation dimension index. From the findings, the range of the level of IFR in the context of presentation dimension is from 41.38 per cent (24 items) to 77.59 per cent (45 items). Based on the table, there is one company (0.36% of the sample) namely Dutaland

Berhad which obtained the lowest IFR presentation dimension. Two companies (0.71% of the sample) namely Boustead Heavy Industries Corporation Berhad and Gamuda Berhad which obtained the highest IFR presentation dimension. Overall, the highest frequency for index disclosure is 32 items (55.17 per cent).

TABLE 6: Level of Internet Financial Reporting for Presentation Dimension

Disclosure Index	No. of Item	Frequency	Percentage (%)
41.38	24	1	0.36
44.83	26	2	0.71
46.55	27	12	4.29
48.28	28	12	4.29
50.00	29	25	8.93
51.72	30	28	10.00
53.45	31	35	12.50
55.17	32	39	13.93
56.90	33	22	7.86
58.62	34	25	8.93
60.34	35	21	7.50
62.07	36	19	6.79
63.79	37	9	3.21
65.52	38	5	1.79
67.24	39	11	3.93
68.97	40	5	1.79
70.69	41	5	1.79
72.41	42	2	0.71
77.59	45	2	0.71
Total	58	280	100.00

Table 7 indicates the results for the IFR disclosure index as an overall. The majority of companies (152 companies; 54.29%) fall under the range from 60 to 69.9. Next, there are 91 companies (32.50%) under the category of 70 to 79.9. Besides, there are 31 companies (11.07%) in the highest range which from 80 to 89.9. Lastly, there are only six companies (2.14%) in the lowest range which IFR index from 50 to 59.9. Based on the previous study conducted by Ali Khan and Ismail (2011), the overall IFR index range is from 40 to 79.9 while the findings of this research have shown an increment from 50 to 89.9. Time factor and the advancement of technology applied by public listed companies might lead to the increase of the level of disclosure of IFR index. The findings of this research also similar to the previous studies conducted by Abdelsalam et al. (2007) and Marston and Polei (2004). The average level of IFR of companies listed on the London Stock Exchange (LSE) as 66 per cent according to Abdelsalam et al. (2007). Based on Marston and Polei (2004), the average level of IFR for companies listed on the Frankfurt Stock Exchange (FSE) in the year 2003 is 67.55 per cent. As a result, based on the findings of this research, the level of IFR for the public listed companies in Malaysia is good.

TABLE 7: Level of Disclosure of Internet Financial Reporting Index

IFR Index	Number of Firms	Percentage (%)
80 – 89.9	31	11.07
70 – 79.9	91	32.50
60 – 69.9	152	54.29
50 – 59.9	6	2.14
Total	280	100.00

Table 8 indicates the IFR items disclosed on companies' website in the context of content dimension. Among the 97 items, there are 16 items present in all the 280 sample companies such as income statement of current year, cash flow statement of current year, balance sheet of current year, income



statement of past years, cash flow statement of past year, balance sheet of past years, statement of changes in shareholders' equity and so on. However, frequently asked question (FAQ), half-year report of current year, information of third party opinion about company, half-year report of past years, monthly or weekly sale or operating data and having a glossary in their website are the items which have less than 10 per cent.



TABLE 8: Internet Financial Reporting Items Disclosed on Companies' Website for Content Dimension

Financial / non-financial disclosure items	Frequency	Percentage (%)
Income statement of current year	280	100.00
Cash flow statement of current year	280	100.00
Balance sheet of current year	280	100.00
Income statement of past years	280	100.00
Cash flow statement of past year	280	100.00
Balance sheet of past years	280	100.00
Statement of changes in shareholders' equity	280	100.00
English version of financial statements	280	100.00
Notes to financial statements of past years	280	100.00
Web page in English	280	100.00
Changes in stockholders' equity in the current year	280	100.00
Current year information can be distinguished from last year's information	280	100.00
Company address	280	100.00
Segmental reporting by region in current year	280	100.00
Company's charter in the current year	280	100.00
Corporate governance principles/guidelines	280	100.00
Text of speeches and presentations	280	100.00
Annual report of current year (full text)	279	99.64
Auditor report of current year	279	99.64
Notes to financial statements of current year	279	99.64
Dividend information	279	99.64
Users quickly find the financial information	279	99.64
Historical share prices	279	99.64
Directors shareholding information	279	99.64
Annual report of current year (excerpt)	279	99.64
Members of the Board of Directors	279	99.64
Chairman's report	279	99.64
Annual general meetings information	279	99.64
Charters for the audit committee	279	99.64
Shareholder information	279	99.64
Past year resolutions of shareholders' meeting	279	99.64
Annual report of past years (full text)	278	99.29
Accounting policy	278	99.29
Segmental reporting by line of business in current year	278	99.29
Corporate information	278	99.29



Information regarding a dividend reinvestment plan	278	99.29
Information on corporate strategy	278	99.29

Financial / non-financial disclosure items	Frequency	Percentage (%)
Segmental reporting by line of business in past years	278	99.29
Current year resolutions of shareholders' meeting	278	99.29
Corporate social responsibility report	278	99.29
Past year resolutions of the Supervisory Board	278	99.29
Charters of others committees	278	99.29
Auditor report of past years	277	98.93
Current year resolutions of the Board of Directors	277	98.93
Postal address to investor relations	277	98.93
Past year resolutions of the Board of Directors	277	98.93
Information about managers, at least the identity and curriculum vitae of executives	276	98.57
Current year resolutions of the Supervisory Board	276	98.57
Employee shareholding information	276	98.57
Management report/analysis in current year	275	98.21
Analyses of main business risks	275	98.21
Top 10 stockholders in current year	275	98.21
Segmental reporting by region in past years	275	98.21
Summary of annual report of current year	274	97.86
Indicator for finding current information directly	274	97.86
Annual report of past years (excerpt)	274	97.86
Code of conduct and ethics for directors, officers and employee	274	97.86
Sales of key products	272	97.14
Projected information	272	97.14
Phone number to investor relations	270	96.43
E-mail to investor relations	268	95.71
Current press releases or news	265	94.64
Supplement or amendment to current year annual report	257	91.79
Summary of financial data over a period of at least five years	208	74.29
Link to Bursa Malaysia websites	208	74.29
Information on intellectual capital	207	73.93
Summary of key ratios over a period of at least five years	199	71.07
Recent monthly financial data	199	71.07
Financial ratios	197	70.36
Indication of audited and unaudited information (half yearly and quarterly)	195	69.64



Quarterly report of current year	189	67.50
Information on the date of latest websites update	187	66.79
Number of share traded	170	60.71
Malaysian Financial Reporting Standards (MFRS) basis in the current year	169	60.36
Classes of shares	168	60.00

Financial / non-financial disclosure items	Frequency	Percentage (%)
Quarterly report of past years	154	55.00
Current share prices	139	49.64
Share quote	135	48.21
Listing of analysts following the firm	127	45.36
Monthly share prices	116	41.43
Specific update time for the stock/share price data	107	38.21
Share price performance in relation to stock market index	105	37.50
Share price graphs	102	36.43
Option provided to register for future email alerts regarding press releases, newsletters, etc.	101	36.07
Calendar of events of interests to investors	94	33.57
Calendar of future financial activities	90	32.14
CEO signature in the report	47	16.79
Auditor signature in past years report	45	16.07
Disclaimer	45	16.07
Auditor signature of current year	43	15.36
Other than English web page (such as Malay)	28	10.00
Frequently Asked Question (FAQ)	18	6.43
Half-year report of current year	11	3.93
Information of third party opinion about company	11	3.93
Half-year report of past years	10	3.57
Monthly or weekly sale or operating data	6	2.14
Glossaries	3	1.07

Table 9 shows the IFR items disclosed on companies' website in the context of presentation dimension. Among the 58 items, there are eight items present in all the 280 sample companies such as annual report in PDF format, loading time of the website below 10 seconds, link to homepage, link to top homepage and so on. However, among the 280 sample of companies, hyperlinks to data on a third-party's website, hyperlinks inside the annual report, sound files, financial data in processable format (such as Excel), service to change data in the share register online, conferences, hyperlinks to financial analysts, help information/site, financial information can be viewed in more than one currency (UK£ & US\$) and having a chat room in their website are the items less than 10 per cent.



TABLE 9: Internet Financial Reporting Items Disclosed on Companies' Website for Presentation Dimension

Financial / non-financial disclosure items	Frequency	Percentage (%)
Annual report in PDF format	280	100.00
Loading time of the website below 10 seconds	280	100.00
Link to homepage	280	100.00
Link to top homepage	280	100.00
Change to printing friendly format possible	280	100.00
Clear boundaries for annual reports	280	100.00
Users can compare and analyses comparative stock or other performance on the same screen	280	100.00
Menu pull-down	280	100.00
Ability to download reports	279	99.64
Format of reports suitable for calculations	279	99.64
Next/previous bottoms to navigate sequentially	279	99.64
Hyperlinks texts	279	99.64
Annual meeting	279	99.64
Menu click over	279	99.64
Graphic images	279	99.64
Table of content/sitemap	278	99.29
Mail listings	278	99.29
Use of multimedia technology (in general)	277	98.93
One click to get to investors relations information	276	98.57
Content can be viewed in different browsers (Internet Explorer and Netscape)	276	98.57
External links to related content	275	98.21
Link to table of contents	273	97.50
Use of frames	272	97.14
One click to get to press releases or news	271	96.79
Users have a choice of download (black and white or full colour)	271	96.79
Direct e-mail hyperlinks to investor relations	267	95.36
Direct e-mail contacts (feedback) available	265	94.64
Moving picture such as JAVA applications	218	77.86
There is information concerning technical devices (formats, size of downloads)	150	53.57
Online feedback	136	48.57
E-mail alerts	124	44.29
Users can download the full annual reports in sections	116	41.43
Flashes	104	37.14
User can subscribe to public announcement via e-mail	93	33.21
Annual report in multiple file format	83	29.64



Contact to the webmaster	73	26.07
Notice book	68	24.29
Online investor information order service	67	23.93

Financial / non-financial disclosure items	Frequency	Percentage (%)
Internal search engine	52	18.57
Technical hints for the user (browsers, screen resolution)	45	16.07
Online shareholder services available (e.g. change address, dividend paid directly into account)	41	14.64
There are investment calculators available (e.g. investment return or dividend calculator)	39	13.93
Function to recommend the page	34	12.14
Annual report in HTML format	33	11.79
Use of presentation slides	33	11.79
Users can download the financial information in more than one type of format	31	11.07
Download plug-in on spot	31	11.07
Video files	29	10.36
Hyperlinks to data on a third-party's website	21	7.50
Hyperlinks inside the annual report	18	6.43
Sound files	15	5.36
Financial data in processable format (such as Excel)	8	2.86
Service to change data in the Share register online	8	2.86
Conferences	7	2.50
Hyperlinks to financial analysts	5	1.79
Help information/site	4	1.43
Financial information can be viewed in more than one currency (UK£ & US\$)	2	0.71



CONCLUSION

The purpose of this research was to study the current status of IFR practices in Malaysia based on the preparer's perception. The content dimension and presentation dimension have illustrated a comprehensive measurement to evaluate the index of IFR disclosed by Malaysian companies. Based on the research findings, the level of IFR started from 55.48 to 85.16 per cent. From the research findings, it can be concluded that the level of IFR among the listed companies in Bursa Malaysia can be declared as 'good disclosers' with regard to the Wallace (1988) index disclosure classification. Besides, similar research has been conducted in previous study and there is an increment of level of IFR in Malaysia listed companies. As a result, this paper is important as it seeks to contribute empirical evidence to the literature regarding the level of IFR in developing countries in general and particularly in Malaysia. In additions, this paper also helped to inform the regulators, investors and stakeholders about the demand of the online information disclosed by the companies.

Apart from that, it is suggested that liable parties such as the Companies Commission of Malaysia (SSM), Securities Commission (SC), Malaysian Institute of Accountants (MIA) and Malaysian Accounting Standards Board (MASB) will come out with a general guideline so that all the companies listed in Bursa Malaysia will able to draw upon when disseminating their corporate and financial information via companies' websites. Besides, this can construct and enhance the uniformity in reporting any related information in the companies' websites used by the listed companies in Bursa Malaysia.

However, even though this research has given serious consideration, there are still a few limitations. Firstly, this research is conducted in the environment of financial reporting in the context of Malaysia. Thus, a comparative research will be vary if similar research conducted in other countries as there are differences between the social background, religion, organizational change, demographic characteristics, financial reporting system, legislative system, cultural factors and management background. Secondly, the research is based on information for the year 2014. Hence, the conclusions reached cannot be generalized. A longitudinal analysis is needed to highlight trends in IFR practices in Malaysia. An in-depth case study would also facilitate our understanding of why companies are making or not making certain types of disclosure of IFR in Malaysia. Thirdly, this research is a cross-sectional research. As a result, it is unable to evaluate the effect with regards to time changes and this can only be done through longitudinal research. However, the use of quantitative and qualitative techniques in cross-sectional research will aid in understanding the direction of IFR practice for companies listed in Bursa Malaysia from time to time.

Finally, it is hoped that the findings of this research will be helpful to related party and also encourage having more related studies in empirical evidence. The researchers also hope that the findings of this research will able to increase the knowledge of the community such as preparers of financial reports, users of financial reports, consumers, proprietors, industry experts, legislators, accounts legislators, researchers, other professional bodies, government, regulators, policy makers, standard setters, corporations, market participants, management and other institutions on the IFR practice.

ACKNOWLEDGEMENT

I would like to express our heartfelt appreciation to Prof. Dr. Noor Azizi Ismail (UUM) for their valuable and constructive suggestions during the planning and development of this research as part of his advisory. My special thanks are extended to Faculty of Management, Universiti Teknologi Malaysia and Research Management Centre, Universiti Teknologi Malaysia for providing the grant for the research work under Research University Grant (RUG) Tier 1 Q.J130000.2529.09H11. The author also gratefully acknowledges the contribution of Norhayati Salleh and Ho Shuang Tien for completing this manuscript.



REFERENCES

- Abd. Aziz, N.H., Mohd Iskandar, T., & Mohd Saleh, N. (2006). Pengurusan perolehan: Peranan kualiti audit dan urus tadbir korporat. *International Journal of Management Studies*, 13(Special Issue), 163-188.
- Abdelsalam, O.H., & Street, D.L. (2007). Corporate governance and the timeliness of corporate internet reporting by U.K. listed companies. *Journal of International Accounting, Auditing and Taxation*, 16, 111-130.
- Abdul Hamid, F.Z. (2005). Malaysian companies' use of the internet for investor relations. *Corporate Governance: The International Journal of Business in Society*, 5(1), 5-14.
- Abdul Hamid, F.Z., Md Salleh, M.S., & Mohamad, R. (2006). A survey of the use of internet for the investor relations by the Malaysian and Singapore firms. Unpublished Research Report. Sintok, Malaysia: Universiti Utara Malaysia, School of Accounting.
- Al Arussi, A.S., Selamat, M.H., & Mohd Hanefah, M. (2009). Determinants of financial and environmental disclosures through the internet by Malaysian companies. *Asian Review of Accounting*, 17(1), 59-76.
- Aly, D., Simon, J., & Hussainey, K. (2010). Determinants of corporate internet reporting: evidence from Egypt. *Managerial Auditing Journal*, 25(2), 182-202.
- Ali Khan, M.N.A. (2010). *Pelaporan Kewangan menerusi Internet: Indeks, Tahap Pelaporan dan Faktor Penentunya*. Unpublished PhD Dissertation: Universiti Utara Malaysia, Sintok, Kedah.
- Ali Khan, M.N.A., & Ismail, N.A. (2011). The level of internet financial reporting of Malaysian companies. *Asian Journal of Accounting and Governance*, 2, 27-39.
- Ali Khan, M.N.A. & Ismail, N.A. (2012). An empirical evidence of the indexes of internet financial reporting: The case of Malaysia. *African Journal of Business Management*, 6(5), 2086-2100.
- Ali Khan, M.N.A. & Ismail, N.A. (2013). An Empirical Investigation of Selected Aspects on Internet Financial Reporting in Malaysia. *Jurnal Teknologi*, 64(3), 39-47.
- Ali Khan, M.N.A. & Ismail, N.A. (2014). Determinants of Web Based Financial Reporting in Malaysia. *GIABR Journal of Business*, 1(1), 28-56.
- Bartulovic, M., & Pervan, I., (2014). Determinants of voluntary Internet Financial Reporting: analysis for selected CEE countries. *International Journal of Economics and Statistics*, 2, 32-39.
- Bonson, E., & Escobar, T. (2006). Digital reporting in Eastern European: an empirical study. *International Journal of Accounting Information System*, 7, 299-318.
- Bue, G.T., Hassan, M.S., & Md. Nor, H. (2008). Kerelevanan nilai pelaporan segmen di Malaysia. *Jurnal Pengurusan*, 27, 21-47.
- Camfferman, K., & Cooke, T.E. (2002). An analysis of disclosure in the annual reports of U.K. and Dutch companies. *Journal of International Accounting Research*, 1, 3-30.
- Chan, W.K., & Wickramasinghe, N. (2006). Using the internet for financial disclosure: the Australian experience. *International Journal Electronic Finance*, 2(1), 118-150.
- Curuk, T. (2008). An analysis of the companies' compliance with the EU disclosure requirements and corporate characteristics influencing it: A case of Turkey. *Critical Perspectives on Accounting*, available at: doi:10.1016/j.cpa.2007.05.003 (assessed 6 August 2008).
- FASB. (2000). *Business reporting research project: Electronic distribution of business reporting information*. Steering Committee Report Series, Financial Accounting Standards Board.
- Gowthorpe, C. (2000). Corporate reporting on the internet: developing opportunities for research. *Journal of Applied Accounting Research*, 5(3), 3-29.
- Hanifa, M.H., & Ab. Rashid, H. (2005). The determinants of voluntary disclosures in Malaysia: the case of internet financial reporting. *UNITAR E-Journal*, 2(1), 22-42.
- Haniffa, R.M., & Cooke, T.E. (2002). Culture, corporate governance and disclosure in Malaysian corporations. *ABACUS*, 38(3), 317-349.
- Hashim, F., & Mohd Saleh, N. (2007). Voluntary annual report disclosures by Malaysian multinational corporations. *Malaysian Accounting Review*, 6(1), 129-156.



- Hassan, S, Jaaffar, N., Johl, S.K., & Mat Zain, M./N. (1999). Financial reporting on the internet by Malaysian companies: perceptions and practices. *Asia-Pacific Journal of Accounting*, 6(2), 299-319.
- Hossain, M., Lin, M.T., & Adams, M. (1994). Voluntary disclosure in annual reports of New Zealand companies. *Journal of International Financial Management and Accounting*, 6(1), 69-85.
- Ilias, A., Abd Razak, M.Z., & Abd Razak, S.F.F. (2014). The Intention to Re-use the Internet Financial Reporting (IFR) in Malaysia. *Review of Integrative Business & Economics Research*, 3(1), 337-370.
- Ismail, N.A., & Tayib, M. (2000). Financial reporting disclosure on the internet by Malaysian public listed companies. *Akauntan Nasional*, 10, 28-33.
- Jain, S.K. & Kumar, P. (2013). Corporate Financial Reporting on Internet – A Study of Users Perception. *Pacific Business Review International*, 5(12), 45-55.
- Keliwon, K., & Aziz, K.A. (2005). Web financial reporting in Malaysia. The current stage, *Proceedings of International Conference on E-Commerce 2005*, Kuala Lumpur, 59-65.
- Kelton, A.S., & Yang, Y. (2008). The impact of corporate governance on Internet financial reporting. *Journal of Accounting and Public Policy*, 27(1), 62-87.
- Khadaroo, M.I. (2005). Business reporting on the internet in Malaysia and Singapore: A comparative study. *Corporate Communications: An International Journal*, 10(1), 58-68.
- Khan, T. (2006). *Financial Reporting Disclosure on the Internet: An International Perspective*. Unpublished doctoral dissertation, Victoria University, Footscray Park, Victoria, Australia.
- Krejcie, R.V., & Morgan, D.W. (1970). Determining sample size for research activities. *Educational and Psychological Measurement*, 30, 607-610.
- Ku Ismail, K.N.I., & Chandler, R. (2004). The timeliness of quarterly financial reports of companies in Malaysia. *Asian Review of Accounting*, 12(1), 1-18.
- Lymer, A., Debreceny, R., Gray G. L., & Rahman A. (1999). *Business Reporting on the Internet*. The International Accountings Standards Committee (IASC).
- Marston, C., & Polei, A. (2004). Corporate reporting on the internet by German companies. *International Journal of Accounting Information System*, 5, 285-311.
- Mohamad, R., Saad, S., Ismail, S.A., & Abdul Rahman, A. (2006). Malaysian corporate website: a survey of web characteristics. Paper presented at *International Conference on ICT for the Muslim World (ICT4M) 2006*, Kuala Lumpur, November 21-23, 2006.
- Mohd Ghazali, N.A., & Weetman, P. (2006). Perpetuating traditional influences: Voluntary disclosure in Malaysia following the economic crisis. *Journal of International Accounting, Auditing and Taxation*, 15, 226-248.
- Mohd Isa, R. (2006). Graphical information in corporate annual report: a survey of users and preparers perception. *Journal of Financial Reporting & Accounting*, 4(1), 39-60.
- Naser, K. (1998). Comprehensiveness of disclosure of non-financial companies. *International Journal of Commerce and Management*, 8(1), 88-119.
- Naser, K., Al-Khatib, K., & Karbhari, Y. (2002). Empirical evidence on the depth of corporate information disclosure in developing countries: The case of Jordan. *International Journal of Commerce Management*, 12(3/4), 122-155.
- Oyelere, P., Laswad, F., & Fisher, R. (2003). Determinants of internet financial reporting by New Zealand companies. *Journal of International Financial Management and Accounting*, 14(1), 26-61.
- Poon, P.L., Li, D., & Yu, Y.T. (2003). Internet financial reporting, *Information Systems Control Journal*, 1, 1-3.
- Purba, L., Medyawati, H., Silfianti, W. & Hermana, B. (2013). *Internet Financial Reporting Index Analysis*, 1(3), 281-284.
- Rahmat, M.M., & Mohd Iskandar, T. (2004). Audit fee premiums from brand name, industry specialization and industry leadership: A study of the post Big 6 merger in Malaysia. *Asian Review of Accounting*, 12(2), 1-24.
- Shiri, M., Salehi, M. and Bigmoradi, N. (2013). Internet financial reporting: Case of Iran. *Journal of Distribution Science*, 11(3), 49-62.
- Sriram, R.S., & Lakshmana, I. (2006). Corporate web site reports: some evidence on relevance and usefulness. *Information Resources Management Journal*, 19(3), 1-17.



- Topalian, A. (2003). Experienced reality, the development of corporate identity in the digital era. *European Journal of Marketing*, 37(7/8), 1119-1132.
- Trabelsi, S., Labelle, R., & Laurin, C. (2004). CAP forum on e-business: the management of financial disclosure on corporate websites: a conceptual model. *Canada Accounting Perspectives*, 3(2), 235-259.
- Uyar, A. (2012). Determinants of corporate reporting on the internet An analysis of companies listed on the Istanbul Stock Exchange (ISE). *Managerial Auditing Journal*, 27(1), 87-104.
- Wallace, R.S.O. (1988). Corporate financial reporting in Nigeria. *Accounting and Business Research*, 18(72), 352-362.

Department of Accounting and Finance
Faculty of Management
Universiti Teknologi Malaysia
81310 UTM Johor Bahru, Johor
MALAYSIA



DETECTING EARNINGS MANIPULATION BY MALAYSIAN PUBLIC LISTED COMPANIES: THE RELIABILITY OF BENEISH M- SCORE MODEL

MOHAMAD EZRIEN BIN MOHAMAD KAMAL
MOHD FAIRUZ MD SALLEH
AZLINA AHMAD

School of Accounting, Faculty of Economics and Management
Universiti Kebangsaan Malaysia
43600, Bangi, Selangor
MALAYSIA
mohdezrien@yahoo.co.uk

Abstract

In detecting financial reporting fraud and manipulation, various financial statement fraud prediction tools have been developed in prior studies. Among them is the Beneish M-Score model which has been recognised as a financial forensic tool to assist in evaluating the probability of earnings manipulation in a company. The model was found to accurately identify potential earnings manipulators in 76% of the public listed corporations subjected to the accounting enforcement actions of the United States Securities and Exchange Commission (U.S. SEC), using only publicly available financial statement data. The current study attempts to assess the reliability of the Beneish M-Score model in detecting earnings manipulation in Malaysian public listed companies. The sample for this pilot study consists of 17 public listed companies whom their directors and top management have been charged and prosecuted by the Securities Commission Malaysia (SC) for committing fraudulent reporting and misstatement from 1996 until 2014. The results shows that the Beneish M-score model is a reliable tool in predicting potential earnings manipulation by 82% in 14 out of the 17 listed companies identified by the SC to be engaging in fraudulent reporting and misstatement. The findings provide support for the application of the Beneish M-Score model by prospective and existing shareholders to reduce the risk of investment losses due to fraud. In addition, the findings suggest that the model can also be applied by researchers, auditors and enforcement agencies as an effective investigative tool to detect potential fraudulent reporting companies in Bursa Malaysia for further analysis and remedial actions.

Key Words: Earnings Manipulation, Beneish M-Score model, Fraudulent Financial Reporting.



INTRODUCTION

Financial reporting fraud can negatively affect capital markets due to erosion in investors' confidence, while damaging the company's reputation towards the point of extinction (Center for Audit Quality, 2010). Such implications also include significant losses of shareholders values due to abnormal stock price decline, bankruptcy, delisting from stock exchange and material assets sales upon fraud discovery (COSO, 2010). Furthermore, according to a report by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in year 2010, there were 347 alleged cases of public company fraudulent financial reporting from 1998 to 2007, as opposed to 294 cases from 1987 to 1997 in the United States. This statistic was contributed amongst others by the high-profile frauds in Enron, WorldCom, and other firms bringing about the total cumulative misstatement or misappropriation of nearly USD120 billion across 300 fraud cases. Malaysia also has its share of high-profile corporate fraudulent reporting scandals, as evidenced in the enforcement action taken by the Malaysian Securities Commission and its public media releases. Among the recent high-profile Malaysian fraudulent financial reporting cases were Megan Media Holdings Bhd, Mems Technology Berhad, Transmile Group Bhd, Axis Incorporation Berhad and Silver Bird Berhad which resulted in total misstatement worth billions of ringgit.

Fraudulent reporting can be caused by deliberate manipulation of earnings in company's financial statement beyond the accounting rules to fulfil the corporate's expectations of achieving favourable performance and profitability (Bedard & Johnstone, 2004; Beneish, 1999; ISA240, 2009). According to Magrath and Weld (2002), such act of earnings manipulation would involve abusive earnings management scheme and fraudulent accounting practice which penetrated the borderline of accounting standards. The 2010 COSO report identified two common techniques used which are improper revenue recognition and asset over statement, with improper revenue recognition representing majority of the fraudulent reporting cases by 61%. Experience have proven that fraud related to preparation of financial statement and disclosure can be extremely difficult to uncover without the assistance of corporate insider (US Securities and Exchange Commission, 2014). Nevertheless various prediction models have been developed utilising financial statements data to assist in the detection of earnings manipulation, leading towards fraudulent reporting. Among them is the Beneish M-Score model which has been recognised as a financial forensic tool to assist in evaluating the probability of earnings manipulation in a company. The model was found to accurately identify potential earnings manipulators in 76% of the public listed corporations subjected to U.S. SEC's accounting enforcement actions, using only publicly available financial statement data (Beneish, 1999).

The current study attempts to assess the reliability of the Beneish M-Score model in detecting earnings manipulation among Malaysian public listed companies in the year prior to being caught and investigated by the Malaysian Securities Commission for committing fraudulent financial reporting. The sample for this pilot study consist of 17 public listed companies, whom their directors and top management have been charged and prosecuted by Malaysian Securities Commission from 1996 until 2014. The test reveals that 14 out of 17 of these companies (82%) were identified by the model to be earnings manipulators. The findings provide strong evidence on the significant benefit of utilising the Beneish M-Score model to detect Malaysian public listed companies that manipulate their earnings and having very high likelihood of potentially committing fraudulent reporting, susceptible towards the Malaysian SC's investigation and enforcement. Thus, the findings will be contributively



valuable towards the potential users of financial statements such as the prospective and existing shareholders, financier, auditors, forensic investigator and academic researcher in considering using the Beneish M-Score model not just to identify earnings manipulating companies for assisting in their decision making and planning, but to also potentially predict companies that later can be prosecuted and charged for fraudulent reporting.

This paper proceeds as follows; the literature review related to earnings manipulation and fraudulent financial reporting as well as the Beneish M-Score Model is elaborated on in the next section followed by methodological issues pertinent to this study. Next, the results are presented and discussed, followed by conclusion and suggestion for future research.

LITERATURE REVIEW

1. Earnings Manipulation and Fraudulent Financial Reporting

Earnings manipulation in financial statements can lead towards non-compliance with accounting rules and standards, resulting into fraudulent financial reporting (Bedard & Johnstone, 2004; Beneish, 1999; ISA240, 2009; Magrath & Weld, 2002).

Dechow, Sloan and Sweeney (1996) investigated the potential motivations for earnings manipulation and whether there is any relationship between earnings manipulation and weaknesses in firm's internal governance structure on a sample of firms subjected to US SEC's accounting enforcement actions for alleged violations of Generally Accepted Accounting Principles. The study found that an important motivation for earnings manipulation is the desire to attract external financing at low cost and firms that manipulated earnings are more likely to have boards of directors dominated by the management, and having a Chief Executive Officer who simultaneously serves as Chairman of the Board. In a similar study, Summers and Sweeney (1998) found that in the presence of fraud, insiders reduce their holdings of company stocks through high levels of selling activity as measured by the magnitude of shares sold. They also reported that fraud companies have more inventories relative to sales, have fast growth level and have higher return on assets than no-fraud firms in the year before the occurrence of fraud.

Two main studies examining earnings manipulation relative to fraudulent reporting were carried out by Beneish (1997) and Beneish (1999). Beneish (1997) scrutinised 49 firms subjected to US SEC's Accounting and Auditing Enforcement Releases (AAER) and another 15 firms with questionable accounting practice by the news media from 1987 to 1993, which were categorised as manipulators. In line with his objective of distinguishing between manipulators and aggressive accruals, another group of companies were categorised as aggressive accruals. These companies were identified based on the modified Jones model. The study revealed that accruals, day's sales in receivables, and prior performance are significant for explaining the differences between manipulators and aggressive accruals. Beneish (1999) later developed a model to distinguish manipulators from non-manipulators by utilising financial statements variables. He matched 74 companies that manipulated earnings with 2,332 COMPUSTAT non-manipulators based on two-digit SIC industry and year. He then calculated an index for eight



financial statement ratios being analysed, with higher index values indicating potential earnings manipulation. The study also revealed that day's sales in receivables index, gross margin index, asset quality index, sales growth index, and accruals are significant in explaining manipulation, which later lead him to develop a probit model with probability cut offs that reduce the expected costs of misstatements. The model was found to accurately identify potential earnings manipulators in 76% of the public listed corporations subjected to the U.S. Securities and Exchange Commission's (SEC) accounting enforcement actions.

Dechow, Ge, Larson, and Sloan (2011) examined financial characteristics of misstating firms and developed a model to predict misstatement by compiling a database of firms subjected to enforcement actions by the U.S. SEC for allegedly misstating their financial statements. They found that at the time of misstatements, accrual quality is low and both financial and non-financial measures of performance declined. Furthermore off-balance sheet financing are more likely to take place during misstatement periods and managers of misstating firms appear sensitive to their firm's stock price. The researchers also developed a composite measure of the likelihood of manipulation (F-score) that can be used as a red flag or signal of the likelihood of earnings management or misstatement. The F-scores model was later used to predict misstatement in a holdout sample of firm-years from 1999 till 2002, which correctly identifies misstating firms by 51.4 percent.

Bell, & Carcello (2000) who tested a sample of 77 fraud firms and 305 non-fraud firms and developed a logistic regression model that estimates the likelihood of fraudulent financial reporting for an audit client, conditioned on the presence or absence of several fraud-risk factors. They reported that weak internal control environment; rapid company growth; inadequate or inconsistent profitability; undue emphasis on meeting earnings projections by management; management lied to the auditors or was overly evasive; the ownership status (public vs. private) of the entity; and mix of weak control environment and aggressive management attitude towards financial reporting are significantly related to fraudulent reporting. These significant variables were then incorporated in their predictive model. In most cases, firms which were bankrupt were found to also commit earnings manipulation which may amount to fraudulent reporting prior to bankruptcy year. Such a situation suggest that the management of the bankrupt firms were under pressure to the extent of having incentive to manipulate the financial statements to ensure the firms concerned can still operate without having to be liquidated. This was supported by Rosner (2003) who have tested on 293 bankrupt firms to examine whether their pre-bankruptcy financial statements more likely to display material income increasing earnings manipulation as compared to non-bankrupt firms. The result indicated that bankruptcy firms' financial statements prior to the year of bankruptcy do not show any sign of financial distress and reflect significantly greater material income increasing level as compared to non-bankruptcy control firms. Furthermore these firms display significant material increase in receivables; inventories; property, plant and equipment, sales, net working capital, current and discretionary accruals, and more significant negative changes in cash flow from operations and net cash compared to non-bankrupt firms (Rosner, 2003). Liou (2008), analysed whether the same financial factors being used in the business failure prediction (BFP) models can also be significantly used in detecting fraudulent financial reporting. The result indicated that many financial factors are significant to both models of business failure and fraud detection. Thus he concluded that financial distress firms are more likely to have fraudulent financial statement, in line with Rosner (2003).



Skousen and Wright (2008) investigated a comprehensive set of contemporaneous firm fraud risk factors identified from the fraud triangle theory as described in SAS No. 99 and past literatures. The variables were tested using a matched-pair sample of fraud firms and non-fraud firms and found that the proportion of independent audit committee members is inversely related to the incidence of fraud. Furthermore they also found that when the proportion of ownership held by managers already holding more than 5 percent of the outstanding shares increases, the likelihood of fraud increases; and when the percentage of insider ownership already holding less than 5% outstanding shares declines, the likelihood of fraud rises. In addition they also suggested that the frequency of fraud is greater among firms that have board duality and do not have an audit committee.

Lou and Wang (2009) examined potential fraud risk factors of the fraud triangle for pressure/incentive, opportunity, and rationalization/attitude and its ability in assessing the likelihood of fraudulent financial reporting. They found that several variables categorised as financial pressure (such as analysts forecast error, debt ratio), variables under management financial pressure (such as directors' and supervisors' stock pledged ratio), variables under rationalisation (such as percentage of sales related party transaction, number of historical restatements prior to fraud) and variables under opportunity (such as number of auditor switch) to be significant. The results indicate that fraudulent reporting is positively correlated to firm's higher financial pressure, higher percentage of complex transactions, higher questionable integrity, and higher deterioration in relation between a firm and its auditor. However the study did not find any significant relationship between board duality with fraudulent financial reporting which contradicted the findings of Skousen and Wright (2008) and Dechow et al. (1996).

Companies which are facing financial distress and managing its earnings excessively are more likely to commit fraudulent reporting. This is evidenced in a study by Hasnan, Abdul Rahman and Mahenthiran (2013) who examined how management rationalization measured by related-party transactions, history of prior violations and number of founders on the board; management motive measured by financial distress, ownership incentives, and political connections; and opportunity measured by the absence of strong corporate governance mechanisms in Malaysian public listed companies result in an environment that leads to fraudulent financial reporting. Furthermore they also studied whether fraud firms engaged in earnings management up to five years prior to the fraud year. Their study found that firms with fewer related-party transactions, a higher number of prior violations, and with founders on the board are more likely to commit fraudulent financial reporting. In addition, they found that firms are involved in fraudulent financial reporting when ownership is not in the hands of the family or foreign shareholders, and the propensity for fraudulent reporting is high when financial distress is high. In addition they also found firms involved in fraudulent reporting do not have strong corporate governance mechanisms and engaged in earnings management two to three years prior to the fraud year. The findings on earnings management was also supported by Perols and Lougee (2011) who found that firms that have previously managed earnings are more likely to commit fraud. Furthermore they also concurred that firms that meet or beat analyst forecasts and firms with inflated revenue are more likely to be committing fraud even when they have not managed earnings in prior years.



Extensive literatures are available on factors causing fraudulent financial reporting and earnings manipulation among public listed companies. A few studies have also investigated on the significance of the fraud risk factors laid down by fraud triangle theory in affecting the fraudulent reporting occurrence with various beneficial findings. In addition, numerous predictive models to detect potential fraudulent reporting and earnings manipulation have been introduced with differing successful detection rate. The Beneish M-Score has received more attention due to its high successful detection rate of earnings manipulation and its ability in uncovering high-profile corporate fraudulent reporting scandals in the United States by analysing companies' financial statement data in two years. Furthermore it has been extensively used and taught in the United States as evidenced in many articles written for the practitioners and in text books. Nevertheless the reliability of the detection model such as the Beneish M-Score is only limited to the US environment and not formally extended to other regions including the South East Asian region. Thus this study attempts to prove the reliability of the Beneish M-Score model in detecting earnings manipulation committed by the Malaysian public listed companies charged and prosecuted by the Securities Commission for fraudulent financial reporting.

2. Beneish M-Score Model

In 1999, Professor Messod D. Beneish has developed a model to distinguish manipulators from non-manipulators by utilising the financial statements variables. Prior to the development of the model, he created a profile of firms that were identified as earning manipulators. The model consisted of 8 ratios utilised to capture either financial statement distortions that can result from earnings manipulation or to identify an inclination to engage in earnings manipulation. The model, well known as Beneish M-Score Model is as follows:

$$\text{M-Score} = -4.84 + 0.92\text{DSRI} + 0.528\text{GMI} + 0.404\text{AQI} + 0.892\text{SGI} + 0.115\text{DEPI} - 0.172\text{SGAI} + 4.679\text{TATA} - 0.327\text{LVGI}$$

The details of the eight variables recognised as indices are stated as follows:

DSRI	Days' Sales in Receivables Index. This measures the ratio of days' sales in receivables versus prior year as an indicator of revenue inflation.
GMI	Gross Margin Index. This is measured as the ratio of gross margin versus prior year. A firm with poorer prospects is more likely to manipulate earnings.
AQI	Asset Quality Index. Asset quality is measured as the ratio of non-current assets other than plant, property and equipment to total assets, versus prior year. It intends to measure the company's risk propensity to capitalise cost.
SGI	Sales Growth Index. This measures the ratio of sales versus prior year. While sales growth is not itself a measure of manipulation, the evidence suggests that growth companies are likely to find themselves under pressure to manipulate in order to keep up appearances.
DEPI	Depreciation Index. This is measured as the ratio of the rate of depreciation versus prior year. A slower rate of depreciation may mean that the firm is revising useful asset life assumptions upwards, or adopting a new method that is income friendly.
SGAI	Sales, General and Administrative expenses Index. This measures the ratio of SGA expenses



	to the prior year. This is used on the assumption that analysts would interpret a disproportionate increase in sales as a negative signal about firms' future prospects
LVGI	Leverage Index. This measures the ratio of total debt to total assets versus prior year. It is intended to capture debt covenants incentives for earnings manipulation
TATA	Total Accruals to Total Assets. This assesses the extent to which managers make discretionary accounting choices to alter earnings. Total accruals are calculated as the change in working capital accounts other than cash less depreciation. It measures a risk relating to accrual policies being used as financing mechanism for losses.

The formula used to calculate the Beneish M-score's indices are as follows:

DSRI	=	$\frac{\text{Receivables}_t / \text{Sales}_t}{\text{Receivables}_{t-1} / \text{Sales}_{t-1}}$			
GMI	=	$\frac{(\text{Sales}_{t-1} - \text{Cost of goods sold}_{t-1}) / \text{Sales}_{t-1}}{(\text{Sales}_t - \text{Cost of goods sold}_t) / \text{Sales}_t}$			
AQI	=	$\frac{(1 - \text{Current Assets}_t + \text{PP\&E}_t) / \text{Total Assets}_t}{(1 - \text{Current Assets}_{t-1} + \text{PP\&E}_{t-1}) / \text{Total Assets}_{t-1}}$			
SGI	=	$\frac{\text{Sales}_t}{\text{Sales}_{t-1}}$			
DEPI	=	$\frac{\text{Depreciation}_{t-1} / (\text{Depreciation}_{t-1} + \text{PP\&E}_{t-1})}{\text{Depreciation}_t / (\text{Depreciation}_t + \text{PP\&E}_t)}$			
SGAI	=	$\frac{\text{Sales, general and administrative expense}_t / \text{Sales}_t}{\text{Sales, general and administrative expense}_{t-1} / \text{Sales}_{t-1}}$			
LVGI	=	$\frac{(\text{LTD}_t + \text{Current liabilities}_t) / \text{Total Assets}_t}{(\text{LTD}_{t-1} + \text{Current liabilities}_{t-1}) / \text{Total Assets}_{t-1}}$			
TATA	=	$\frac{\Delta \text{Current Assets}_t - \Delta \text{Cash}_t - \Delta \text{Current liabilities}_t - \Delta \text{Current maturities of LTD}_t - \Delta \text{income tax payable}_t - \text{Depreciation and amortization}_t}{\text{Total assets}}$			

The M-score is used to describe the degree of possible manipulation on earnings and also any other types of fraudulent activity (Mantone, 2013). Furthermore Beneish (1999) found that the M-score model could correctly identifies 76% of the earnings manipulators among the US corporations subjected to SEC's accounting enforcement action. In addition, the model has successfully detected earnings manipulation activities within 71% of companies involved in prominent fraudulent financial reporting cases even before public announcement was made



(Beneish, Lee, & Nichols, 2013). Nevertheless from the financial forensic examiners point of view, the high accuracy percentage of correctly identifying the earnings manipulator will allow for effective and efficient investigation (Mantone, 2013). The models have been used as tools for identifying earnings manipulation and quality in financial statements analysis texts and in articles directed to auditors, certified fraud examiners and investment professionals (Beneish & Nichols, 2007; Golden, Skalak, Clayton, & Pill, 2006; Mantone, 2013; Warshavsky, 2012). The model has also been helpful in assisting certified fraud examiners (CFEs) in detecting signs of financial manipulation and fraud suspicions in firms (Harrington, 2005). Thus the model is an excellent tool for the financial forensic examiner to lead towards further scrutiny of the financial statement changes (Mantone, 2013).

The model's total score indicates the level of probability of financial statement manipulation. A total score greater than -2.22, means that there is a high probability of financial statement manipulation (Beneish 1999; Mantone 2013; Warshavsky 2012). The model's total score has also assisted in identifying potential fraudulent companies prior to enforcement action taken by the authority in the United States such as in the case of Enron (Warshavsky, 2012). In addition to analysing the total score of the model, each of the 8 individual indexes that makes up the Beneish M-score equation can also be independently used to identify any potential manipulation in the financial statement's areas. For instance, Beneish (1999) in his research has come up with a defined threshold for each of the 8 index type of the Beneish M-score model based on the mean score to assist in distinguishing between potential manipulators and non-manipulators.

The defined threshold for the 8 index type based on Beneish (1999) are as follows:

Index Type	Manipulators	Non-Manipulators
Days Sales in Receivables Index	1.465	1.031
Gross Margin Index	1.193	1.014
Asset Quality Index	1.254	1.039
Sales Growth Index	1.607	1.134
Depreciation Index	1.077	1.001
Sales, General, Administrative Expenses Index	1.041	1.054
Leverage Index	1.111	1.037
Total Accruals to Total Assets	0.031	0.018

The Beneish M-score model's indexes are potentially powerful gauges that can assist in further examination of any unexpected results in the company's financial statements (Golden, Skalak, & Clayton, 2006). Nevertheless according to Beneish (1999), the individual indexes are not faultless and can potentially produce inaccurate results. Thus, the underlying components of those indexes may need further evaluation if any of those indexes exceeded the defined threshold above, and the potential for fraud is higher when there is no plausible explanation for the difference (Golden, Skalak, & Clayton, 2006).



Details extracted from two consecutive periods' financial statements (fraud period and prior to fraud period) of the fraudulent reporting companies are applied into the Beneish M-Score model to calculate the overall total score. Any of the companies with the total score greater than -2.22 will indicate high probability of earnings manipulation in financial statement. Furthermore, each of the 8 indexes of the Beneish M-Score model is also generated while calculating the model's total score and to be compared against the defined index threshold as provided by Beneish (1999).

METHODOLOGY

All public companies listed on the Malaysian stock exchange (Bursa Malaysia) that have been identified and charged for committing fraudulent financial reporting by the Malaysian Securities Commission from year 1993 to 2014 were selected as samples for this study. The list of those companies was obtained from the Malaysian Securities Commission's website which provided a comprehensive disclosure of the companies being charged for violations of various Securities Commission Act and Regulations. In order to ensure that the list of companies taken as samples is consistent with the fraudulent financial reporting offence, only those companies that have violated Section 122A, Section 122B, Section 122C, Section 122D of the Securities Industry Act 1983 and Regulation 4 of the Securities Industry (Compliance with Approved Accounting Standards) Regulation 1999 related to fraudulent and misstated financial statements were considered.

Details of all the companies committing various violations of the Securities Commission Act and Regulations were obtained from various sources; (1) Enforcement actions list which is divided into criminal prosecution list, civil actions and regulatory settlements list, cases compounded list and administrative list; (2) Enforcement related press release and; (3) Press release by media. All these sources were accessible from the Malaysian Securities Commission's website. Details of those companies were further reviewed and screened to select only those relevant public listed companies that have violated Section 122A, Section 122B, Section 122C, Section 122D of the Securities Industry Act 1983 and Regulation 4 of the Securities Industry (Compliance with Approved Accounting Standards) Regulation 1999 relevant to the fraudulent and misstated financial reporting offence as samples. Based on the review, 19 public listed companies have been found to have committed fraudulent financial reporting in violation of the Securities Commission Act and Regulations between 1993 to 2014. Relevant quarterly and final year's financial statements for two consecutive periods (fraud period and period prior to fraud) related to those 19 fraudulent reporting companies were obtained from the Bursa Malaysia's website. Two out of 19 fraudulent reporting companies were excluded from the samples as one was found of committing fraudulent reporting within the same year after getting listed on Bursa Malaysia and the other was due to inadequate financial statement data for the application of the Beneish M-Score model. To detect earnings manipulation, the model requires two consecutive periods of the company's financial statements data; the period when the fraud is committed and the prior period. This leaves a final sample of 17 public listed companies related to fraudulent reporting to be examined for earnings manipulation using the Beneish M-Score model. Data extracted from the relevant fraudulent and misstated financial statements for two consecutive periods were used to calculate the Beneish M-Score total based on the following model:



$$\text{M-SCORE} = -4.84 + 0.92\text{DSRI} + 0.528\text{GMI} + 0.404\text{AQI} + 0.892\text{SGI} + 0.115\text{DEPI} - 0.172\text{SGAI} + 4.679\text{TATA} - 0.327\text{LVGI} \quad (1)$$

The results of the Beneish M-score total calculation for every fraudulent reporting companies were-observed and documented. The results then were analysed to determine the number and percentage of fraudulent reporting companies scoring greater than -2.22, and to prove the reliability of the Beneish M-Score model in detecting high probability of earnings manipulation in financial statements before fraud and misstatement being detected by the Malaysian Securities Commission. Furthermore, 8 indexes that build up the Beneish M-Score model were also analysed for every fraudulent reporting companies against the defined index threshold as provided by Beneish (1999).

EMPIRICAL RESULTS

Table 1 provides the results of the calculation of Beneish M-score and its 8 indexes for the 17 sample companies. Table 2 displays descriptive statistics results for the Beneish M-Score, including its 8 indexes and Table 3 shows the percentage of fraudulent reporting companies having the total Beneish M-Score greater than -2.22.

No	Mistatement yr	Company	DSRI	GMI	AQI	SGI	DEPI	SGAI	LVGI	TATA1	MSCORE
1	2011	Silver Bird Bhd	1.40	1.23	0.93	1.22	0.99	0.80	1.00	0.05	-1.56
2	2007	Mems Tech Bhd	0.70	1.13	1.36	1.07	1.44	0.77	3.24	-0.13	-3.76
3	2007	LFE Corp Bhd	1.03	0.40	0.79	1.19	0.54	0.68	0.91	0.03	-2.53
4	2007	Axis Incorp Bhd	1.02	1.03	0.83	1.26	0.83	0.50	1.04	0.12	-1.65
5	2007-2006	Oilcorp Berhad	1.50	1.53	0.88	2.90	0.86	0.62	1.16	0.02	-0.02
6	2007	Talam Corporation Berhad	2.60	-0.49	1.02	0.36	0.96	0.75	1.00	-0.03	-2.48
7	4th quarter 2006	Inix Technologies	0.23	1.19	0.48	6.95	0.42	1.14	0.57	0.16	2.82
8	dec06/qtrs07	Satang Hold Bhd	1.17	0.91	0.48	1.26	0.52	1.02	1.41	0.33	-1.02
9	2006	Kosmo Tech Ind Bhd	1.87	1.06	2.27	1.13	0.45	1.78	1.04	0.10	-0.78
10	2006	Megan Media Hold Bhd	1.65	0.95	0.86	1.14	0.91	0.92	1.04	-0.02	-1.93
11	4th quarter 2006	Transmile Group Bhd	1.91	0.88	0.89	1.80	1.00	1.43	0.81	0.08	-0.70
12	2005	Nasioncom Hold Bhd	2.18	1.05	0.78	1.21	0.77	0.98	1.21	0.17	-0.56
13	2005	Welli Multi Corp Bhd	0.99	1.38	0.92	1.30	0.72	0.70	1.02	0.06	-1.76
14	2004	United U-Li Corp Bhd	1.09	1.00	1.00	1.23	0.95	0.91	1.13	0.15	-1.53
15	4th quarter 2004	Goh ban Huat Berhad	0.93	1.60	0.64	0.91	1.13	2.41	0.65	0.33	-1.01
16	2004	Aktif Lifestyle Berhad	0.84	0.33	26.61	0.01	4.95	1.80	0.10	14.28	73.92
17	2003	Polymate Hold Bhd	1.33	0.87	0.45	1.21	0.66	0.95	1.05	0.11	-1.81

TABLE 1: Total M-Score for the companies with fraudulent and misstated financial statements

As stated in table 3, fourteen (82%) out of seventeen fraudulent reporting companies were found to have total M-score higher than -2.22. This shows that the Beneish M-score model is capable of detecting earnings manipulation



committed by 82% of the fraudulent reporting companies. Thus the model is potentially useful for identifying companies having the likelihood of being prosecuted for fraudulent reporting in violation of the Malaysian Securities Commission Act and Regulations. This is slightly higher than Beneish's (1999), which reported 76% success rate in detecting fraudulent reporting US companies as included in the US SEC's Accounting and Auditing Enforcement Releases (AAER's).

Three of the fraudulent companies scoring the highest M-score totals are Aktif Lifestyle Berhad (73.92), followed by Inix Technologies Berhad (2.82) and thirdly by Oilcorp Berhad (-0.02). The company with the highest M-score also have the highest index score above the defined threshold determined by Beneish (1999) in the area of Asset Quality Index (AQI=26.61), Depreciation Index (DEPI=4.95), and Total Accrual to Total Assets (TATA=14.28), causing the total M-score to exceed above the -2.22 threshold, indicating severe earnings manipulation. Further investigation also revealed that Aktif Lifestyle Berhad had earlier been charged in 2004 for failure to comply with approved accounting standards, specifically FRS 122 on business combination which resulted in material misstatements in the financial statements to the extent of being issued with adverse audit report. Inix Technologies Berhad, the company with the second highest M-score, also scored the highest for Sales Growth Index (SGI=6.95), and above median score for its Sales, General, Administrative Expenses Index (SGAI = 1.14) and Total Assets to Total Accruals (TATA=0.16). Furthermore, Inix Technologies Berhad had submitted false statement to the Bursa Malaysia for the year ended December 2006, with its revenue being overstated.

	DSRI	GMI	AQI	SGI	DEPI	SGAI	LVGI	TATA1	MSCORE
Mean	1.32	0.94	2.42	1.54	1.06	1.07	1.08	0.93	3.16
Median	1.17	1.03	0.88	1.21	0.86	0.92	1.04	0.10	-1.53
Max	2.60	1.60	26.61	6.95	4.95	2.41	3.24	14.28	73.92
Min	0.23	-0.49	0.45	0.01	0.42	0.50	0.10	-0.13	-3.76
Index threshold limit	1.47	1.19	1.25	1.61	1.08	1.04	1.11	0.03	
No of companies above threshold limit	6	4	3	3	3	5	5	12	
% of companies above threshold limit	35%	24%	18%	18%	18%	29%	29%	71%	

TABLE 2: Descriptive statistics for the Beneish M-Score total and indexes

No of M-score > -2.22	14
Comp with mistatement	17
% of M-score > -2.22	82.35%

TABLE 3: % of M-score > -2.22

With reference to Table 2, 12 companies (71%) were found to have Total Accruals to Total Assets (TATA) score higher than the threshold limit of 0.03. The result showed the highest count for the number of companies breaching



the TATA score threshold limit as compared to other indexes, indicating potential high manipulation on the companies' accrual policies which can be associated with higher likelihood of earnings manipulation. The second individual index of the Beneish M-score with the highest number of companies breaching the threshold limit is Days Sales Receivables Index (DSRI) with 6 (35%) of the fraudulent reporting companies detected of exceeding the 1.47 threshold limit. This suggest that the 6 companies may have overstated their revenue, resulting in earnings manipulation. The third high score index is shared together by Leverage Index (LVGI) and Sales, General, Administrative Index by having 5 (29%) fraudulent companies respectively exceeding their threshold limit. Gross Margin Index (GMI) falls at the fourth place with 4 (24%) of the fraudulent companies breaching its threshold limit and followed lastly by 3 indexes of AQI, SGI and DEPI with 3 (18%) fraudulent reporting companies respectively exceeding the threshold limit, indicating potential manipulation. Based on the Beneish M-score model, 5 of the main indexes can have significant weightage in pushing the companies' M-score higher than -2.22, being led by TATA at 4.679 times, secondly DSRI at 0.920 times, thirdly SGI at 0.892 times, fourthly GMI at 0.528 times and finally AQI at 0.404 times.

CONCLUSION

Firms' earnings manipulation can lead towards fraudulent financial reporting, resulting in detrimental effect towards the stakeholders in various means. The outcome of earnings manipulation will generate misleading and materially misstated financial statements, prone towards erroneous decision making causing significant amount of losses to the related parties including the company committing such manipulative act. The confidence level on companies committing earnings manipulation relative to fraudulent reporting will decline drastically resulting in potential bankruptcy. Nevertheless earnings manipulation leading to fraudulent reporting is difficult to established, thus various earnings manipulation detection tools and fraud predictive models have been developed to assist the stakeholders in evaluating the trustworthiness of the financial statements issued. One of the detection tools that has made the attention is the Beneish M-Score model which has been reliably used as a financial forensic tools to predict earnings manipulation in financial statements. Furthermore the detection model is widely discussed and taught in the United States as evidenced in professionals' articles, academic text books and reference materials. The formal reliability of the model is yet to be seen in country such as Malaysia, though well proven in the U.S.

The study's findings reveal that 82% of the sampled public listed companies related to fraudulent financial reporting and misstatement have been found of committing earnings manipulation during the fraud year by the Beneish M-score model. Thus, the model is proven to be reliable for identifying companies having the likelihood of being prosecuted for fraudulent reporting in violation of the Malaysian Securities Commission Act and Regulations.

The study findings will be contributively valuable towards the potential users of financial statements such as the prospective and existing shareholders, financier, auditors, forensic investigator and academic researcher in considering using the Beneish M-Score model not just to identify earnings manipulating companies for assisting in



their decision making and planning, but to also predict companies that later can be prosecuted and charged for fraudulent reporting. Furthermore, better understanding can be obtained on the attributes of the earnings manipulating companies as a proxy for the actual detected and non-detected fraudulent reporting companies as compared to using only those companies already charged and prosecuted by the enforcement agencies. This is because, the actual number of prosecuted companies is normally small and might neglect the non-prosecuted fraudulent reporting companies which still remain at large, resulting in difficulty in generalising the accurate nature and characteristics of all companies committing fraud and misstatement. Most of the prior researches identified fraudulent reporting firms from the list of enforcement actions for fraud and restatement made by the respective authority such as the securities commission. Such list neglected the potential fraudulent reporting companies that still remain undetected. Thus it is possible for the no-fraud firms to have committed fraud but they have yet to be detected. Furthermore, the authority such as SEC may have selection biases in fraud cases to be pursued based on firms' stock performance decline and the large amount of losses suffered by investors, resulting in most firms that have manipulated earnings to remain undetected. Thus the usage of the Beneish M-score model would overcome this issue. Some limitations of this study are as follows. Firstly, the Beneish M-Score model according to Beneish's (1999) can incorrectly classify 24% of manipulators as the non-manipulators while having the tendency to misclassify 17.5% of the non-manipulators as earnings manipulators. Secondly, the model can only be used to analyse the financial statement data of the public listed companies only and cannot be reliably used in the private limited companies' environment.

Future research should attempt to study the attributes of the potential earnings manipulators identified by the model and whether they are linked to fraud risk factors. Furthermore the corporate governance mechanism adopted by these potential earnings manipulators should be examined further for comparison against the accepted code of practice.

References:

- Bedard, J. C., & Johnstone, K. M. (2004). Earnings Manipulation Risk , Corporate Governance Risk , and Auditors' Planning ... *The Accounting Review*, 79(2), 277–304.
- Bell, T. B., & Carcello, J. V. (2000). A Decision Aid for Assessing the Likelihood of Fraudulent Financial Reporting. *AUDITING: A Journal of Practice & Theory*, 19(1), 169–184. doi:10.2308/aud.2000.19.1.169
- Beneish, M. D. (1997). Detecting GAAP violation: implications for assessing earnings management among firms with extreme financial performance. *Journal of Accounting and Public Policy*, 16(3), 271–309. Retrieved from <http://linkinghub.elsevier.com/retrieve/pii/S0278425497000239>
- Beneish, M. D. (1999). The Detection of Earnings Manipulation. *Financial Analysts Journal*, 55(5), 24–36. doi:10.2469/faj.v55.n5.2296
- Beneish, M. D., Lee, C. M. C., & Nichols, D. C. (2013). Earnings Manipulation and Expected Returns. *Financial Analysts Journal*, 69(2), 57–82. doi:10.2469/faj.v69.n2.1



- Beneish, M. D., & Nichols, D. C. (2007). Predictable Cost of Earnings Manipulation. Available at SSRN: <http://ssrn.com/abstract=1006840>, (August). doi:10.2139/ssrn.1006840
- Center for Audit Quality. (2010). *Deterring and Detecting Financial Reporting Fraud; A platform for action* (p. 55). Retrieved from www.TheCAQ.org
- COSO. (2010). *Fraudulent Financial Reporting: 1998 - 2007, an analysis of U.S. Public Companies Committee of Sponsoring Organizations of the Treadway Commission* (pp. 1–60).
- Dechow, P. M., Ge, W., Larson, C. R., & Sloan, R. G. (2011). Predicting Material Accounting Misstatements. *Contemporary Accounting Research/Recherche Comptable Contemporaine*, 28(1), 17–82. doi:10.1111/j.1911-3846.2010.01041.x
- Dechow, P. M., Sloan, R. G., & Sweeney, A. P. (1996). Causes and consequences of earnings manipulation: An analysis of firms subject to enforcement actions by the SEC. *Contemporary Accounting Research*, 13(1), 1.
- Golden, T. W., Skalak, S. L., & Clayton, M. M. (2006). *A Guide to Forensic Accounting Investigation* (pp. 378–383). John Wiley & Sons Inc.
- Golden, T. W., Skalak, S. L., Clayton, M. M., & Pill, J. S. (2006). *A guide to forensic accounting investigation. Choice Reviews Online* (Vol. 43). John Wiley & Sons. doi:10.5860/CHOICE.43-6636
- Harrington, C. (2005). Formulas for detection Analysis ratios for detecting financial statement fraud. *Fraud Magazine*.
- Hasnan, S., Abdul Rahman, R., & Mahenthiran, S. (2013). Management Motive, Weak Governance, Earnings Management and Fraudulent Financial Reporting: Malaysian Evidence. *Journal of International Accounting Research*, 12(1), 1–27. doi:<http://dx.doi.org/10.2308/jiar50353>
- ISA240. (2009). International Standard on Auditing 240 The auditor's responsibilities relating to fraud in an audit of Financial Statements (pp. 155–197).
- Liou, F. M. (2008). Fraudulent financial reporting detection and business failure prediction models: a comparison. *Managerial Auditing Journal*, 23(7), 650–662. doi:10.1108/02686900810890625
- Lou, Y., & Wang, M. (2009). Fraud risk factor of the fraud triangle assessing the likelihood of fraudulent financial reporting. *Journal of Business & Economics ...*, 7(2), 61–78. Retrieved from <http://journals.cluteonline.com/index.php/JBER/article/viewArticle/2262>
- Magrath, L., & Weld, L. G. (2002). Abusive Earnings Management and Early Warning Signs. *The CPA Journal*, 0802(August). Retrieved from www.nysscpa.org/cpajournal/2002/0802/features/fo85002
- Mantone, P. S. (2013). *Using Analytics to Detect Possible Fraud Tools and Techniques*. John Wiley and Sons.
- Perols, J. L., & Lougee, B. a. (2011). The relation between earnings management and financial statement fraud. *Advances in Accounting*, 27(1), 39–53. doi:10.1016/j.adiac.2010.10.004



- Rosner, R. L. (2003). Earnings Manipulation in Failing Firms*. *Contemporary Accounting Research*, 20(2), 361–408. doi:10.1506/8EVN-9KRB-3AE4-EE81
- Skousen, C. J., & Wright, C. J. (2008). Contemporaneous Risk Factors and The Prediction of Financial Statement Fraud. *Journal of Forensic Accounting*, IX, 37–62.
- Summers, S. L., & Sweeney, J. T. (1998). Fraudulently misstated financial statements and insider trading: An empirical analysis. *The Accounting Review*, 73(1), 131.
- US Securities and Exchange Commission. (2014). Financial Reporting and Audit Task Force. Retrieved from <http://www.sec.gov/spotlight/finreporting-audittaskforce.shtml>
- Warshavsky, M. (2012). Earnings Quality. *Financial Valuation and Litigation Expert*, (39), 16–20.

MOHD FAIRUZ MD SALLEH, Ph.D.

School of Accounting, Faculty of Economics and Management

Universiti Kebangsaan Malaysia

43600, Bangi, Selangor

MALAYSIA

AZLINA AHMAD, Ph.D.

School of Accounting, Faculty of Economics and Management

Universiti Kebangsaan Malaysia

43600, Bangi, Selangor

MALAYSIA



THE IMPLEMENTATION AND DISCLOSURE OF CORPORATE SOCIAL RESPONSIBILITY (CSR) IN INDONESIAN BANKING INDUSTRIES

RINA TRISNAWATI

Accounting department, Economics and Business Faculty,
Universitas Muhammadiyah Surakarta
Jl A Yani Tromol pos 1 Pabelan Surakarta, Central Java,
INDONESIA
rina.trisnawati@ums.ac.id

Abstract

Corporate Social Responsibility (CSR) is a concept that companies have responsibility not only on the environment within the company's operations, but also have a responsibility to customers, employees, shareholders, and communities. The previous studies for CSR disclosure used GRI index (78 items) have done by many researchers (Almilia and Retrinasari, 2007; Anggraini, 2006; Febrina and Suaryana, 2011; Rahman and Widyasari, 2008; Sembiring, 2005 Veronica, 2008). They did CSR disclosure in manufacturing industries in Indonesia. The implementation of GRI index in banking industries is done by Trisnawati (2011), Fitria and Hartanti (2010). The result showed the conventional banks are better CSR disclosure than shariah banks

The purpose of this study is to investigate the disclosure of corporate social responsibility (CSR) in conventional and shariah banking industries in Indonesia during 2009-2011 periods. This research used Global Reporting Initiative (GRI) index with adjusted model for disclose CSR in these companies. We used 90 items GRI based on convergence between GRI (121 item) and ISR. (Trisnawati,2012). The most measurement which had done is CSR disclosure from Global Reporting Initiative (GRI) with 72 items (Fitria and Hartanti, 2010), 78 items (Sembiring, 2005; Trisnawati, 2011), 79 items (Febrina and Suaryana, 2011), 121 items (Permatasari, 2012). Their results showed that CSR disclosure is limited score

The sample are 7 conventional banks and 5 shariah banks listed companies in Indonesia which reported annual report in 2009-2011 periods. The data analysis used content analysis and descriptive method to identify dimension and implementation of social responsibility disclosure among these banks. The scoring used 1, if banks disclosed these GRI items and 0 if they are not disclosed. The scored each banks showed the rate of CSR disclosure. Then, the implementation of CSR practice by identified the activities CSR each banks based on their publications and describe the real CSR disclosure from each sample. The result showed that the conventional banking industries got the higher score than shariah banks. The higher getting score, it means they have more social responsibility to their communities based on GRI index. It looked at from 10 indicators such as (1) analysis and strategies (2) profile (3) reporting indicators, (4) governance, (5) economic performance, (6), environment, (7) social performance, (8) employment ,(9) communities and (10) product responsibility.

Key words: Banking industries, Corporate Social Responsibility, convergence GRI and ISR

1. INTRODUCTION

The financial report is a information for stakeholders. With the issuance of the financial statements can provide a variety of information about the performance of the company as well as the activity of a company. The information provided in the financial statements used by investors, creditors, potential investors, potential creditors



and other users for decision making. The information presented is complete, accurate and timely lets investors make decisions rationally. One of the information currently as the focus by the investor is information about corporate social responsibility (CSR).

Corporate Social Responsibility (CSR) is often regarded as the core of business ethics. Company has financial obligation to shareholders and shareholders also have an obligation to other parties such as consumers, employees, communities and the environment around the company. Awareness of the importance of corporate social responsibility disclosure is based on the premise that companies have not only economic and legal obligations only to shareholders, but the obligation to others also interested. Since the company's commitment is to contribute in nation building by always give attention to the financial aspects (economic), social and environmental aspects or often called the triple bottom line (Purwanto, 2011).

Corporate Social Responsibility (CSR) is the theoretical basis of the need for a company to build a harmonious relationship with the community and environment in which it operates. Theoretically, CSR can be defined as a moral responsibility towards the stakeholders of the company, especially to the community or communities in which their operations. The success of a company in the viewpoint of CSR is to promote the moral and ethical principles, namely to reach the best results, without harming other communities (Febrina and Suaryana, 2011).

Based on the Capital Markets Law No.8: 1995 paragraph 1, "the material information or the important and relevant facts regarding events, or facts which may affect the price of securities on the Stock Exchange, and or the investor's decision, prospective investors or the others who have an interest in such information "(Sembiring, 2005). Accounting researchers also began to articulate various different theoretical perspectives in the social accounting support, such as the decision usefulness studies, studies of economic theory, and social and political theory. The rule about CSR in Indonesia stipulated in Undang-Undang R.I No.40 tahun 2007 pasal 74 ayat (1) about the Limited Company. This regulation states that: "The Company is conducting its business activities in the field and/or related to the natural resources required to carry out social and environmental responsibility".

Based on this regulations CSR, is not voluntary disclosure to the company, it has become mandatory disclosure. It means, CSR is a reflection of the need for accountability for the disclosure of the company's social responsibility, so the stakeholders can assess the company activity. Previously had been discussed, CSR is not only related to the environmental issues but also ethical and moral issues. Castello and Lima (2006) state that CSR relates to ethical and moral issues of how companies make decisions and behave. It also addresses issues such as environmental protection, human resource management, health and safety in the workplace, relationships with local communities and relationships with suppliers and customers.

Generally, reporting standards which are well known for implementing CSR is the GRI index (Global Reporting Initiative). GRI is an organization that has pioneered the development of CSR and sustainability



reporting using the framework and is committed to continuously make improvements and implementation across in the world ([www. Globalreporting.org](http://www.Globalreporting.org)). Research on CSR with GRI index has been used extensively by several researchers (Almilia and Retrinasari, 2007; Anggraini, 2006;; Rahman and Widyasari, 2008; Sembiring, 2005;Veronica, 2008). These studies did in the manufacturing industry in Indonesia using the GRI index (78 items). Febrina and Suaryana (2011) using 79 items, Then, Permatasari (2012) using 121 items based on GRI reporting in 2011.

The implementation Application of GRI in the banking industry have also been carried out by previous research. Fitria and Hartanti (2010), conducted a study of three conventional banks and Islamic banks. The results showed that CSR disclosure in conventional banks are better than Islamic banks. Based on GRI index, the highest value of 46% and based on the ISR index by 58%. The measurement used is GRI index (121 items) and Islamic Social Reporting (ISR) (72 items) which developed by AAOIFI. Trisnawati (2011) conducted an analysis of CSR disclosure in conventional and Islamic banks in Indonesia using the GRI index 78 item. The research findings are consistent with Fitria and Hartanti (2010) that CSR disclosure in conventional banks are better than the Islamic bank is 52% and 37%. Subsequently Trisnawati, et.al (2013) conducted an analysis of CSR disclosure in Islamic banks in Indonesia with ISR index. Results showed that the disclosure of the ISR by 50.68%

Research in the CSR , especially in sharia banking industries generally used the Islamic Social Reporting (ISR) index developed by AAOIFI. Later, it developed by some researchers (Hanifa, 2002; Maali, et. Al, 2006; Ousama and Fatima, 2006; Solomon, 2005 ; Othman, et. al, 2009). In particular index ISR is an extension of social reporting which includes not only the expectations of the public about the role of firms in the economy, but also the company's role in the spiritual perspective (Haniffa, 2002). Research related to the disclosure of CSR in Islamic banks in Indonesia by using an index developed ISR AAOIFI has done Fitria and Hartanti (2010); Hasan and Harahap (2010); Sofyani et.al (2012); Azhar and Trisnawati (2013) Various studies show that the measurements using the GRI index (72 items, 78 items, 79 items, and 121 items) does not show a maximum score of disclosure, the value of disclosure average below 50%. This research is designed to perform CSR disclosure in the banking industry in Indonesia because it is not optimal score based on the index of CSR disclosure. The index used is adjusted GRI index (90 items with 10 supplement). This refers to the study Trisnawati et al. (2013) to perform content analysis and decomposition analysis of the GRI index 121 items and ISR.

2. LITERATURE REVIEW

2.1. CSR Reporting in Indonesia

Based on a survey conducted by the Global Reporting Initiative (2008), it is found a significant increase the number of companies making CSR report, known as sustainability reporting which was from about 300 firms in



1996 to 3100 firms in 2008. In addition, the survey also shows that CSR reporting is mostly done as voluntary and not mandatory disclosure. Therefore, sustainability reporting forms and formats vary considerably according to the needs of the organization. It becomes reasonable considering the number of international organizations that have provided guidance to present CSR reporting such as: the Global Reporting Initiative Sustainability Reporting Guidelines (published by the Global Reporting Initiative (GRI)), the Organization for Economic Cooperation and Development guidelines for multinational enterprises (published by the Organization for Economic Cooperation and Development (OECD)), Social Accountability 8000 (published by Social Accountability International), AA 1000 for auditing and assurance process (published by Accountability, an international membership organization), Environmental management systems (ISO 14001, EMAS), *the* Global Compact and United Nations norms, (published by the United Nations), as well as the Greenhouse Gas Protocol (published by the World Business Council for Sustainable Development (WBCSD) and the World Resources Institute). Among the various reporting standards reported, the GRI Sustainability Reporting Guidelines are the accepted standard of reporting in general and most widely used by companies in the world. In Indonesia, the CSR is the most widely applied concept in strategic level companies in Indonesia and the community felt the need for companies to do CSR activities (Swa, 2005). Empirical research also shows that an increase in social disclosure in corporate annual financial statements Indonesia (Fitria and Hartanti 2010). And the increasing number of companies in Indonesia that uses *the* Global Reporting Initiative standards in CSR reporting (Darwin, 2007).

2.2. The concept of Corporate Social Responsibility

According to Fitria and Hartanti (2010), the concept of CSR as a corporate social responsibility is widely accepted. Although there are several parties who consider it is still controversial, they argued that the profit company has to pay a sum of money in the form of taxes to the state for distribution to the public in order to improve welfare. Meanwhile, the opposing parties stating that the company cannot be separated from the individuals involved in it, such as owners and employees. Therefore, it is not the time for companies only think of financial gain only, but also must care for the rights and interests of the public, especially around the company. Until now, there is no fixed definition of social responsibility, each side has different definitions and interpretations of CSR. In general, CSR can be defined as responsibilities undertaken by the company to its stakeholders to behave ethically and comply with all aspects of economic, social and environmental well-for sustainable development (Fitria and Hartanti 2010). In terms of conventional philosophy, there are several theories behind the implementation of CSR in companies, namely:



1. **Milton Friedman's Capitalism Theory.** According to Friedman (1967) if the company's CSR activities in the outside of the shareholder interests, then it violates the company's goals. The company has to provide prosperity to the shareholders. Donation activity allowed if deemed to provide benefits for the company.
2. **Social Contract Theory.** In this theory believed that the company can only be tried better if it is supported by the community (Moir, 2001). So, the company will be regarded as a social institution that must contribute to their social environment.
3. **Instrument Theory.** According to this theory, CSR is strategies to achieve company goals. So, according to this theory, firms conducted CSR activities have a specific purpose such as creating a positive reputation, public relations or other similar benefits. (Burke and Logsdon, 1996).
4. **Legitimacy Theory.** According to this theory, the company will conduct CSR activities due to social pressures, politics and economy from outside the company. So, the company will balance these demands by doing what the people wanted and what is required by regulation (Darus et al, 2008).
5. **Stakeholder Theory.** According this theory, The CSR activity made to accommodate the desires and needs of stakeholders (stakeholders) so that companies can move increasingly by the support these stakeholders (Clarkson, 1995).

The World Business Council for Sustainable Development (WBCSD) in its publication defines CSR or Corporate Social Responsibility, as: "Continuing commitment by business to be ethically and have contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at ". The WBCSD has a statement about CSR disclosure, it is a form of commitment in the corporate world to continuously act ethically, operating legally and contribute to economic development, along with improving the quality of life of employees and their families as well as improving the quality of the local community and society more broadly. (Karina, 2011)

The World Bank defines CSR as the commitment of business to contribute to sustainable economic development, working with employees, their families, local communities and society as a whole to improve the quality of their lives for the better, so that is good for business and good for development. Broader definition of CSR, as recommended by the World Bank, including the following principles: (1) CSR is voluntary; (2) CSR exceed existing regulations; (3) CSR is about social and environmental issues in key business practices, such as environmental management, labor standards, fair relationships with customers and others; (4) CSR is not a donation or philanthropy. The most important is mutually beneficial scenario for the business and its stakeholders; (5) a complement rather than a replacement CSR regulations. (Arifiyanto, 2013)

Theoretically CSR can be defined as a company's moral responsibility towards the stakeholders particularly the community around the work area and operations. A company must uphold morality. The success of



a company's CSR viewpoint is focus on moral and ethical principles, to achieve the best results, without harming society. CSR is based on three principles, known as the triple bottom lines by Eklington (Ahzar, 2012), namely:

(1). Profit.

Profit is an important element and the main goal of business activity. The company remains to be oriented to seek economic advantage allows it to continue for operating. Activities that can be taken to reach profits by greatly increasing the productivity and cost efficiency, so the company has a competitive advantage that can provide added value as possible.

(2).People.

The company should have concern for human welfare. Recognizing that the community around the company is one of the important stakeholders for the company, because of the support of the local community is necessary for existence, survival, and development of the company. So as an integral part of the community environment, companies need to be committed to working to provide maximum benefit to the community. For example, the provision of scholarships to students about the company, the establishment of educational and health facilities, and strengthening the capacity of the local economy.

(3). Planets.

The company's relationship with the environment is a causal relationship, whereby if the companies take care of the environment, then the environment will benefit the company. The company's obligation to care for the environment and sustainable biodiversity. For example, greening the environment, housing improvement, and the development of tourism (ecotourism). That is, CSR should be able to increase its profit, welfare of employees and the community, while improving environmental quality.

Ambadar (2008) suggests some of the motivation and the expected benefits to the company doing corporate social responsibility include: 1) the company avoid the negative reputation that only environmentally destructive pursuit of short-term profits regardless of the result of the bad behavior of the company, 2) a strong ethical framework can help managers and employees face problems such as employment demand in the environment in which the company works, 3) the respect of the company's core group of people who require the existence of the company, especially in terms of job creation, 4) ethical behavior of the company safe from the surrounding environment where they operate.

Untung (2008) revealed several benefits of CSR for companies, namely: (1) Maintaining and increase reputation and brand image of the company, (2) Obtaining a license to operate socially, (3) Reduce the risk of the company's business, (4) Expanding access to resources for business operations , (5) Opening wider market opportunities, (6) reduce costs, for example the impact of waste disposal, (7) Improving relationship with stakeholders, (8) Improving relationships with regulators, (9) Improving employee morale and productivity, (10) opportunity awarded.



From some of definition CSR above, it can be concluded that CSR is a form of corporate social responsibility actions with moral and ethical principles in sustainable economic development in order to improve the quality of life and environment that are beneficial, both for the company itself, the local community, and society.

3. RESEARCH METHODOLOGY

The population of this research is all of the conventional banks which listed in Indonesian banks industries during 2009-2011 periods. Based on data from www.bi.go.id, there are 123 banks listed in Indonesian banking industries. They are one (1) bank as central bank, four (4) state-owned banks, 33 private domestic commercial banks / BUSN Exchange (Three of them are Islamic banks such as Bank Muamalat Indonesia, Bank Syariah Mandiri and Bank Mega Syariah), 33 National Private Banks / non-foreign BUSN (two of them are Islamic bank :BRI syariah and BUKOPIN syariah), 26 regional banks, 17 joint venture banks, 9 foreign banks and 5 Islamic banks.

The sample used in this study are 7 (seven) conventional banks in Indonesia. It is selected by total assets. This study was designed through a survey to obtain annual financial statements banks during 2009-2011. Based on a survey of Bank Indonesia in May 2011, there are seven large banks (total assets owned Rp.1 - Rp 10 trillion (\$ 117 - \$ 1.17 billion.) Rating banks are in a very good category. They are Bank CIMB Niaga, Bank Rakyat Indonesia, Bank Danamon, Bank Mandiri, Bank Central Asia, Bank Panin and Bank Negara Indonesia 46. These banks are conventional banks listed companies in Indonesia which reported annual report in 2009-2011 periods.

The data analysis used content analysis and descriptive method to identify dimension and implementation of social responsibility disclosure among these banks. The scoring used 1, if banks disclosed these GRI items and 0 if they are not disclosed. The scored each banks showed the rate of CSR disclosure. Then, the implementation of CSR practice by identified the activities CSR each banks based on their publications and describe the real CSR disclosure from each sample. The result showed that the conventional banking industries got the higher score than shariah banks. The higher getting score, it means they have more social responsibility to their communities based on GRI index. It looked at from 10 indicators such as (1) analysis and strategies (2) profile (3) reporting indicators, (4) governance, (5) economic performance, (6), environment, (7) social performance, (8) employment ,(9) communities and (10) product responsibility.



4. EMPIRICAL RESULT

4.1. CSR Disclosure On Islamic bank

Disclosure of Corporate Social Responsibility (CSR) in 5 samples Islamic bank (Bank Muamalat Indonesia, Bank Syariah Mandiri, Bank Mega Syariah, Bank BRISyariah, Bank Syariah Bukopin) were analyzed using the GRI Index (121 items) are reported in table 1 following

Table 1
CSR DISCLOSURE ON ISLAMIC BANKS BASED ON GRI NDEKS (121 ITEMS)

BANKS	2009	2010	2011	MEAN
Bank Muamalat Indonesia	26.45 %	25.62 %	25.62 %	26.04 %
Bank Syariah Mandiri	26.45%	25.62 %	27.27 %	26.45 %
Bank Mega Syariah	22.31 %	18.18 %	19.01 %	19.83 %
BRI syariah	12.40 %	19.01 %	19.83 %	17.08 %
Bank Bukopin Syariah	18.18 %	18.18 %	19.01 %	18.46 %

Source : Trisnawati et al (2013)

Based on the table above, Bank Muamalat Indonesia and Bank Syariah Mandiri CSR revealed more than 26%, while the level of the lowest CSR is BRISyariah by 17:08%. GRI index measurement with 121 items that are based on measurements of Financial Services (3 & G3.1) obtained from <http://database.globalreporting.org/>. The results of this study showed that the average level of CSR disclosure is 21:54%. Based on the GRI adjusted index (Trisnawati et al, 2013), the average level of CSR disclosure increased by 80.06%. This index is done to fix the GRI index measurement by doing convergence between the GRI index (121 items) and the ISR index which developed by AAOIFI (72 items). Furthermore, decomposition analysis done by making adjustments and or delete some items that are not relevant. This means that if all banks do not disclose the item (score 0) then it is not used as a measuring tool. In addition to the other items considered relevant on the basis of the bank's CSR reports and other publications from the bank's website. Doing convergence performed on both the index (after adjustment) by refer with Fitria and Hartanti (2010) and Trisnawati (2012). The results can be seen in Table 2 below.



Table 2

**CSR DISCLOSURE ON ISLAMIC BANKS BASED ON ADJUSTED GRI NDEKS
(90 ITEM +10 SUPPLEMEN)**

BANKS	2009	2010	2011	MEAN
Bank Muamalat Indonesia	83,81%	83,81%	83,81%	83,81%
Bank Syariah Mandiri	85,71%	85,71%	85,71%	85,71%
Bank Mega Syariah	75,24%	76,19%	80,00%	77,14%
BRI syariah	80,00%	80,95%	80,95%	80,63%
Bank Bukopin Syariah	73,33%	72,38%	73,33%	73,02%

Source : Trisnawati et al (2014)

4.2. CSR disclosure on Conventional banking industries.

The results of research on social responsibility disclosure on conventional banks in Indonesia, which is reviewed by using the GRI index which includes 121 items from 2009-2011 periods. The scoring against conventional banks on the existing items as follows:

Table 3

CSR DISCLOSURE ON CONVENTIONAL BANKS BASED ON GRI NDEKS (121 ITEMS)

Nama Bank	2009	2010	2011	Rata-rata
CIMB Niaga	21.49%	23.14%	23.14%	22.59%
BRI	20.66%	22.31%	22.31%	21.76%
Bank Danamon	24.80%	24.80%	24.80%	24.80%
Bank Mandiri	19.01%	18.18%	19.01%	18.73%
BCA	23.14%	23.14%	23.14%	23.14%
Bank Panin	19.01%	19.83%	23.97%	20.93%
BNI	25.62%	26.45%	26.45%	26.17%

Source : Trisnawati et al.(2013)

From the results of the scoring, in 2009 and 2011 shows that the BNI has the highest score, by reaching the percentage per years are 25.62%, 26.45% and 26.45%. It shows, BNI concern towards social responsibility is greater than the other banks when viewed using the GRI index. The other bank that has the lowest score in 2009 through 2011 with the percentage of each years at 19:01%, 18:18% and 19:01%. In addition, if it viewed from an average of the value, the bank with the highest scores is BNI with a score of 26.17% and which has the lowest



score is bank Mandiri which a score by 18.74%. Further, disclosure of CSR conducted by Adjusted GRI index (90 items), which refers Fitria and Hartanti (2010) and Trisnawati (2012). The results can be seen in Table 4 below.

Tabel 4

CSR DISCLOSURE ON CONVENTIONAL BANKS BASED ON
ADJUSTED GRI INDEKS (90 ITEM)

BANKS	2009	2010	2011	MEAN
CIMB Niaga	85,56%	85,56%	85,56%	85,56%
BRI	86,67%	86,67%	87,78%	87,04%
Bank Danamon	84,44%	84,44%	85,56%	84,81%
Bank Mandiri	87,78%	87,78%	87,78%	87,78%
BCA	85,56%	85,56%	86,67%	85,93%
Bank Panin	81,11%	82,22%	83,33%	82,22%
BNI	88,89%	88,89%	88,89%	88,89%

Source ; Trisnawati et al, 2014

The results showed that BNI had the highest score, by reaching percent per year respectively by 88.89% each years. It means BNI concern for social responsibility is greater than another banks which viewed by the GRI index. The result showed that the conventional banking industries got the minimum score is 82.22% and the maximum score is 88.89%. The higher getting score, it means they have more social responsibility to their communities. Based on the adjusted GRI index, the CSR score increasing compare with the 121 GRI index.

4.3. Implementation of CSR

The implementation of CSR in CIMB Niaga Bank focused on education especially the scholarship programs from undergraduate until doctorate level. The others programs are development and social empowerment, cultivate 5000 trees in pantai Indah Kapuk, green office program, filantrophy programs such as give materials for disaster, infrastructure building, blood charity, facilitate employee PGA Volunteer, and Employee Volunteer Club.

Bank Rakyat Indonesia response to their communities by giving the educational scholarship, repairing the school infrastructure, health care for un empowered people, built the health house, bleeding charity, cultivating the productive trees, the cheap market (bazaar) and the socialization of renewing energy such as biogas installation program. BRI allocated more than 100 billion rupiahs for CSR activities.

The CSR programs had done by Danamon bank are “Our market clean will be healthy and wealthy “ implemented in all regions in Indonesia, Danamon go green program, take care for disaster, traditional market revitalization, education for communities to be healthy life. Danamon bank activities focused on economic empowerment by market revitalization on people behavior and market infrastructure.



Bank Mandiri response to their communities by many CSR programs such as educational programs:” Program Kemitraan dan Bina Lingkungan (PKBL)“. It gave scholarship for 20 entrepreneur students. During 2010, Bank Mandiri gave fund amount Rp 5,875 billion for poor people and Rp 3,250 billion for 65 charity organization. Bank Mandiri also gave scholarship for training of trainer amount Rp 968,9 million in Lombok, Aceh, Ambon and Solo. The implementation program of Corporate Social Responsibility (CSR) Bank Mandiri had done by reachment of educational freedom and entrepreneurship.

Bank Central Asia (BCA) did CSR activities on education, health and support the empowerment SME business by forming Organization of Business Development (LPB). BCA also cooperated with United Nations Children’s Fund (UNICEF) for take care children health. In 2010, BCA contributed to educational program by giving scholarship for teachers and undergraduate students and participating in English conference in Bali. BCA also participated with Palang Merah Indonesia (PMI) programs, United Nations Children’s Fund (UNICEF), World Wildlife Fund (WWF), by education banking theme programs. BCA also had contribution for small industries by training management, basic finance, repairing and maintance of vehicles

CSR activities in Bank Panin focused on educational programs, art, health, disaster fund and environment. Panin bank gave scholarship and built school infrastructure. During 2010, Panin bank participated by cultivating 240 juta tress for reducing impact the global warming. Bank Panin response the environment by Green Officer programs. Bank BNI 46 also participated in educational programs, health, children care, empowerment people and care with the environment to reduce pollution and CO2. BNI cooperated with government to educate people for saving money for economic nation growth, participated in Earth Hour 2011 activity and cooperated with Borneo Orangutan Survival Foundation (BOSF) for care the animals.

CSR activities during the period 2009-2011 by Bank Muamalat Indonesia, which provide social assistance to orphans through Baitulmaal Muamalat as the institution concerned with social activities. In addition, Bank Muamalat Indonesia, also distributed Rp 5.686 billion is part of the corporate social responsibility program organized by Baitulmaal Muamalat. As a form of social responsibility, Bank Muamalat also responses to natural disasters through Action Response Muamalat (ATM). This activities such as assistance to victims of Situ Gintung, West Java earthquake victims, and the earthquake in West Sumatra. ATM team also assist isolated areas, during the year 2009 with a total funding USD 3 billion. BMM was carried out in about 75 cities in Indonesia, including Aceh. Compensation given to 72 084 mustahik (classes are eligible to receive compensation). Orphan Kafala Program is a program of community empowerment, especially orphans and the earthquake and tsunami affected families in Aceh. This program is a collaboration of the Islamic Development Bank (IDB) and the Organization of the Islamic Conference (OIC) Alliance. BMM is believed to be implementing this program. Baitulmaal Muamalat (BMM) and the Islamic Financial Services Cooperatives (KJKS) Baitul Maal wa Tamwil (BMT) An-Najah, Pekalongan, Central Java, make a business partner Zakat. BMM also held a socialization program Muamalat Community-Based



Micro Mosque (KUM3). KUM3 is a program providing productive capital to micro entrepreneurs who come from poor families. The participants were worshippers at the mosque around the program area. At the end of the program will be evaluated. KUM3 program successful if it fulfills a number of indicators, such as income micro enterprises increased by at least 70% and 90%. In implementing the plan BMM KUM3 program in eight mosques. Funds are disbursed approximately USD 250 million.

Corporate social responsibility report issued by Bank Syariah Mandiri is expressed in the form of social indicators or charitable assistance. Form of social activity is scholarship aid for Bank Syariah Mandiri sons and daughters. In 2009 BSM also hold social work in Kinah Rejo village which located in the slopes of Mount Merapi, Ground, Yogyakarta. Furthermore, in collaboration with the Institute Amil Zakat BSM, BSM awarded scholarships to 43 children of school at Merapi Slope, Kali Adem mosque renovation assistance, and submit copies of the Qur'an for recitation in mosque Kali Adem, Kinah Rejo village. In social activities associated with organized BSM educational programs designed to increase the capacity of the education one of them is helping to develop human resources Elementary School teachers in Bogor Regency.

Based on Bank Mega Syariah CSR report, the CSR activities is the form of social assistance to the community or people who are less able, such as: orphan (orphanage), elderly parents (nursing home), the homeless, the disabled, victims of disasters and so on. In practice, Bank Mega Syariah is actively seeking employee involvement in this activity, so that the program also educates employees to have a sense of social responsibility and concern for the suffering of others. Besides, it conducting banking education and grants 7 computers for education . Bank Mega Syariah also sympathize 5,000 orphans and the poor, and as many as 100 compensation distributed in Lampung, namely for 100 orphans around the neighborhood office of Bank Mega Syariah. A total of 100 children are less able to receive compensation in the form of gifts and cash, the distribution is centered in the District I Bandar Lampung. In 2010, Bank Mega Syariah Indonesia to distribute zakat via LAZISMU corporation. The partnership is a form of corporate social responsibility. Bank Mega Syariah Indonesia corporate zakat amounted to Rp 2.1 billion.

CSR Disclosure of Bank BRI Syariah leads to indicators related products and services primarily to the activities of Micro, Small and Medium Enterprises (SMEs). In 2010 the disclosure made by the Bank BRI Syariah changed the disclosure in social indicators. One form of social responsibility of Bank BRI Syariah is the national charity information systems (SISN) to the Badan Nasional amil zakat (Baznas). In addition, it supports the implementation of Art Day at the Museum of BI as Bank BRI Syariah effort to preserve the historical value as well as teaching children to love the museum Indonesia.

Bank Bukopin Syariah realize its Corporate Social Responsibility (CSR) in the form of caring. It is obtained based on the report of Corporate Social Responsibility (CSR) which explains that Bank Bukopin Syariah realize CSR programs in the form of compensation. This result is inversely proportional to the value score indicates



that the highest value is expressed in organizational governance indicators. Bank Bukopin Syariah consistently realizing its Corporate Social Responsibility (CSR) in the form of concern for the society, which is packaged with the name "Bukopin Care". CSR commitment embodied by bank Bukopin a pattern that has been applied in the corporate plan. In accordance with the priorities, the social programs are consistently focused on three areas, they are education, health and social welfare of the community. Forms of social care is not only about physical nature, but concern for the improvement of the lives of religious communities and the need to express themselves through sports and cultural arts. In the field of education, Bank Bukopin Syariah continue providing development assistance and renovation of educational facilities, procurement of books and computers, providing scholarships, sponsoring various forms of school competitions as well as to support training activities related communities. For the health sector, bank Bukopin Syariah make the blood donation as a routine tradition, which is followed either by all employees and the surrounding community. It also help of the treatment of patients of underprivileged groups. While concern for the sport by supporting the implementation of the various activities in the community sports tournament.

5. CONCLUSIONS

Result of this study provides evidence that most of Indonesian listed banking industries have disclosed CSR information issues bases on GRI index with 121 items. Eventhough all of banks not disclosed social responsibility and environmental information completely although they reported their annual report during this period. The result indicated that the conventional banking industries got the minimum score is 18.18% and the maximum score is 26.45% and the shariah banks have minimum score 17.08% and maximum score is 26.045. The adjusted GRI index with 90 item has better measurement for CSR disclosure compare with GRI index 121 item. The score CSR is increasing by the new measurement. The conventional banks got the maximum score 88.89% and minimum score is 82.89%. The shariah banks got the maximum score is 85.71% and the minimum score is 73.02%. Generally, the conventional banks have the higher score for CSR disclosure based on these measurement. The result of this study support legitimacy theory in explaining the social responsibility and environmental disclosure by the listed banking industries in Indonesia. The finding was consistent with Darus et al (2008) who argued that regulatory efforts have the prospect of becoming a significant force in promoting the quality of Corporate Social Responsibility (CSR) and environmental disclosure. Generally, the CSR activities concern to social activities such as zakah, shodaqoh fund, empowerment for poor people, help the victim of the disaster, cultivate trees, education fund and health fund. The future researchers should extend the samples by adding Islamic banks as unit analysis and compare them for CSR disclosure. GRI index as tools for measuring CSR disclosure is limited information. Based on the result of this study, the CSR implementation is more information widely that is



not including in GRI items. So, the next studies should repair the GRI items by adding information about education, health, environment issues, children care, empowerment people and other information which these did by companies. The CSR disclosure should be viewed by many information that getting from real companies activities, not only from annual financial statements.

Acknowledgment:

* Thanks for all of team PUPS research (Erma Setiawati, Zulfikar, Mujiyati, Nursiam, Galuh Alvianti, Fahri Ali Azhar, Dimas Bangkit A, Yusuf Abdullah)

REFERENCE

- Almilia, L.S., & Ikka Retrinasari (2007). Analisis pengaruh karakteristik perusahaan terhadap kelengkapan pengaruh dalam laporan tahunan perusahaan manufaktur yang terdaftar di BEJ. *Proceedings Seminar Nasional FE Universitas Trisakti*.
- Ambadar, Jackie, 2008. *Corporate Social Responsibility (CSR) dalam Praktik di Indonesia*. Jakarta: PT. Elex Media Komputindo.
- Anggraini, F.R. (2006). Pengungkapan informasi sosial dan faktor-faktor yang mempengaruhi pengungkapan informasi sosial dalam laporan keuangan tahunan: Study empiris pada perusahaan yang terdaftar di BEJ. *Proceedings SNA IX-Padang*.
- Azhar, F. A, & Trisnawati. (2013). Pengungkapan Islamic social reporting pada bank syariah di Indonesia. *Proceedings, Seminar nasional SANCALL 2013, Fakultas Ekonomi dan Bisnis UMS*, ISBN 878-979-636-147-2.
- Burke, M. C., & Rodrigues, L.C. L. (2006). Communication of corporate social responsibility by Portugese banks: A Legitimacy theory perspective. *Corporate Communication: An International Journal*, 11(3), hal. 232-248.
- Clarkson, A.B., & Dixon, R. (1995). Environmental risk and management strategy: The implications for financial institutions. *The International Journal of Bank Marketing*, 3(2), hal. 22-29.
- Darus, F. 2008. "Influence of institutional pressure and ownership structure on corporate social responsibility disclosure", *Interdisciplinary Journal of Contemporary research in Business*, 1(5), 123-150.
- Deegan, C. (2002), The legitimising effect of social and environmental disclosure – a theoretical foundation, *Accounting, Auditing & Accountability Journal*, Vol. 15 No. 3, pp. 282- 312.
- Fandinata, H. (2012). *Perbandingan perhitungan bunga pada bank konvensional dengan Bank Syariah*. (28 Oktober 2012). Web site: <http://hiskiafandinata.blogspot.com>.



- Febrina & Suaryana, Agung. (2011). Faktor-faktor yang mempengaruhi kebijakan pengungkapan tanggungjawab sosial dan lingkungan pada perusahaan manufaktur di Bursa Efek Indonesia, *Simposium Nasional Akuntansi XIV Aceh*. UNSYIAH.
- Fitria, S., & Hartanti, D. (2010). Islam dan tanggung jawab sosial: Studi menjabarkan perbandingan pengungkapan pelaporan inisiatif global yang berdasarkan indeks dan pelaporan Islamic sosial indeks. *Simposium Pendidikan Nasional Akuntansi XIII Purwokerto*. UNSOED.
- Haniffa, R. (2002). Social reporting disclosure : An Islamic perspective. *Indonesian Management and Accounting Research* 1 (2), hal.128-146.
- Haniffa, R., & Hudaib, M. (2001). A conceptual framework for Islamic accounting: The Shariah paradigm. *International Conference on Accounting, Auditing and Finance*. Palmerstone North, New Zealand, Unpublished article.
- Hasan, A & Harahap, S.S. (2010). Exploring Corporate Social Responsibility disclosure : case of Islamic banks, *International Journal of Islamic and Middle Eastern Finance and Management* Vol. 3 No. 3, pp. 203-227
- Maali, B., Casson, P., & Napier, C. (2006). Social reporting by Islamic Banks. *ABACUS*, 42 (2), hal. 266-289.
- Mansur, S. (2012). *Pelaporan corporate social responsibility (CSR) perbankan Syariah berdasarkan perspektif Syariah enterprise theory*. Skripsi. Fakultas Ekonomi dan Bisnis, Universitas Hasanuddin, Makassar.
- Othman, R., Thani, A. Md., & Ghani, E. K. (2009). Determinants of Islamic social reporting among top Shariah-approved companies in Bursa Malaysia. *Research Journal of International Studies*, 12.
- Ousama, A.A & Fatima, A.H. (2006). *The Determinants of Voluntary Disclosure in the annual reports by shariah approved companies listed in bursa Malaysia*. Paper presented at IIUM International Accounting Conference 3 26-28 June 2006, Kuala Lumpur, Malaysia
- Permatasari, I. (2012). *Analisis karakteristik perusahaan terhadap pengungkapan corporate social responsibility*. E-library UMS/repository/Skripsi/index
- Rahman, A., & Widyasari, K. N., (2008). The analysis of company characteristic influence toward CSR disclosure: Empirical evidence of manufacturing companies listed in JSX. *JAAI*, 12 (1), hal 25.
- Sembiring, E. R. (2005). Karakteristik perusahaan dan pengungkapan tanggung jawab sosial: Studi empiris pada perusahaan yang tercatat di BEJ). *Proceedings SNA VIII*, hal 379-395.
- Sofyani, H., Wahjuni L. S., Ulum, I., & Syam, D. (2012). Islamic social reporting index sebagai model pengukuran kinerja sosial perbankan Syariah: Studi komparasi Indonesia dan Malaysia. *Jurnal Dinamika Akuntansi*, 4 (1), hal. 36-46.
- Suharto, E. (2006). *Membangun masyarakat memberdayakan rakyat: Kajian strategis pembangunan kesejahteraan sosial dan pekerjaan sosial* (edisi ke-2). Bandung: Refika Aditama.



- Sulaiman, M. (2004). Environmental disclosure in Malaysian annual report : A legitimacy theory perspective. *International Journal of Commerce and Management*, 14(1), hal. 44-48.
- Silber, J., & Weber, M. (2009). Labour market discrimination: Are there significant differences between the various decomposition procedures? *Journal Applied Economics*, 31, hal. 351-369.
- Swa, Majalah. (2010). *Membumikan Bisnis Berkelanjutan ; Konsep Dan Praktik Tanggung Jawab Sosial Perusahaan*. www.swa.com.
- Trisnawati, Rina. 2011. *Social Responsibility and Enviromental Disclousure of Annual Report in Banking Sector- Indonesian Listed Companies*. Proceedings, international Conference committee 2010-2011 January 2011, Auditorium UMS.
- Trisnawati, Rina; Fahri Ali Azhar dan Dimas Bangkit A, 2013. *Pengungkapan tanggungjawab Sosial perusahaan (CSR) pada bank Syariah di Indonesia*, Laporan penelitian kolaborasi dosen-mahasiswa, FE UMS, tidak dipublikasikan
- Trisnawati, Rina; Fatchan Ahyani, Zulfikar, Erma Setiawati, Mujiyati, 2013 *Implementasi corporate social responsibility sebagai bentuk tanggungjawab sosial perusahaan (studi komparasi industri perbankan syariah dan konvensional di Indonesia)*. laporan penelitian PUPS tahun 1, LPPM UMS.
- Trisnawati, Rina; Nursiam, Zulfikar, Erma Setiawati, Mujiyati, 2014 *Implementasi corporate social responsibility sebagai bentuk tanggungjawab sosial perusahaan (studi komparasi industri perbankan syariah dan konvensional di Indonesia)*. laporan penelitian PUPS tahun 2, LPPM UMS.
- Trisnawati, Rina. 2012. Pengukuran tanggung jawab sosial perusahaan (CSR) perbankan syariah di Indonesia . *Jurnal Akuntansi dan Auditing Indonesia*. Terakreditasi SK dikti nomor 81/Dikti/Kep/2011. Vol 16 No 2, Des 2012.
- Untari, Lisna, 2010. *Effect on Company Characteristics Corporate Social Responsibility Disclosures in Corporate Annual Report of Consumption Listed in Indonesia Stock Exchange*, Artikel Internet, www.gunadarma.ac.id, diakses tanggal 06 Agustus 2011.
- Untung, Hendrik Budi, 2008. *Coorporate Social Responsibility*, Sinar Grafika. Veronica, T. M. (2008). *Pengaruh karakteristik perusahaan terhadap pengungkapan tanggung jawab sosial pada perusahaan sektor pertambangan yang terdaftar di Bursa Efek Indonesia*. Diakses tanggal 11 Desember 2011, dari www.google.com,
- Veronica, Theodora Martina, 2008. *Pengaruh Karakteristik Perusahaan terhadap Pengungkapan Tanggung Jawab Sosial pada Perusahaan Sektor Pertambangan yang Terdaftar di Bursa Efek Indonesia*, Artikel Internet, www.google.com, diakses tanggal 11 Desember 2011.



**THE EFFECT OF INTERNAL AUDIT QUALITY ON GOOD
UNIVERSITY GOVERNANCE AND ITS IMPLICATIONS ON THE
QUALITY OF EDUCATION OPERATION THAT CONTRIBUTES TO
GRADUATES QUALITY: A CASE STUDY AT PRIVATE HIGHER
EDUCATIONS IN REGION III OF WEST JAVA INDONESIA**

IDA ROSNIDAH

Accounting Department
University of Swadaya Gunung Jati
Jl. Pemuda No. 32 Cirebon West Java
INDONESIA
Idarosnidah2010@yahoo.com

ADI SETIAWAN

Management Department
University of Swadaya Gunung Jati
Jl. Pemuda No. 32 Cirebon West Java
INDONESIA
adi_m2b@yahoo.co.id

MADA PURWANTO WAHYU NUGROHO

Accounting Department
University of Swadaya Gunung Jati
Jl. Pemuda No. 32 Cirebon West Java
INDONESIA
purwantownmada@yahoo.com

DEDI MUHAMMAD SIDDIQ

Management Department
University of Swadaya Gunung Jati
Jl. Pemuda No. 32 Cirebon West Java
INDONESIA
dedisiddiq6@gmail.com

MOH. YUDI MAHADANTO

Accounting Department
University of Swadaya Gunung Jati
Jl. Pemuda No. 32 Cirebon West Java
INDONESIA
mohyudim@yahoo.com



Abstract

Higher education outputs form the basis for nation's civilization. In terms of human resource development, the quality of higher education becomes absolutely necessary to improve the civilization. The quality of higher education operation is analogous to a factory that produces human resources, which contribute significantly to the nation's civilization. There are several variables that theoretically influence the quality of higher education and its graduates that include Internal Audit and Good University Governance. Based on path analysis, it is found that the quality of higher education and its graduates are formed by the presence of Internal Audit and Good University Governance. Referring to the Goodness of Fit Test, it is known that this result can be generalised to the whole population. The populations in this study comprise a number of private universities in Region III of West Java.

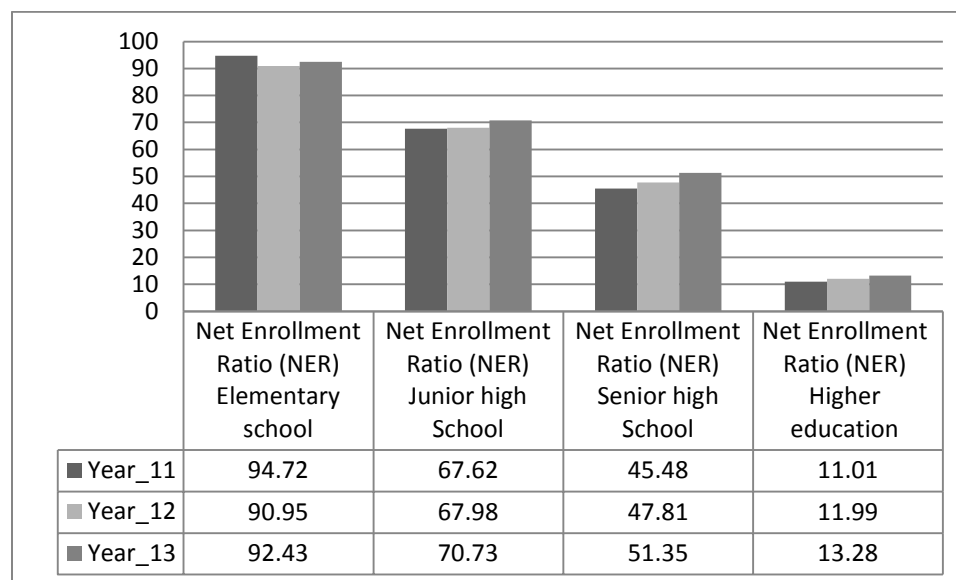
Key Words: Graduate Quality, Quality of Higher Education Operation, Good University Governance and Internal Audit.

INTRODUCTION

1. Background

The quality of education and its implications on the quality of graduates is a central issue in a nation development. University as an institution of higher education has an important role in creating human resources which have the reformer character, intellectual culture and new ideas to seek a solution in addressing the problem (Suhendi, 2013).

The future of a nation will be largely determined by the quality of human resources owned, while the quality of human resources will be determined by how far the level of community participation in educational activities is. Based on the percentage of students with age-related education levels it is found that in the last three years, the number of people who participated in Indonesian universities are much less compared to other educational levels, as shown in Figure 1.



Source: Central Bureau of Statistic 2013

FIGURE 1: The development of Net Enrollment Ratio in Indonesia 2012-2013



Based on the weighted figures of unemployment rate of university graduates in Indonesia using base year 2004, it shows that the highest unemployment rate was in 2010 (see Figure 2). In 2011 to February 2013 despite a decrease in the unemployment rate, it has not reached the level of unemployment rate as the base year 2004.

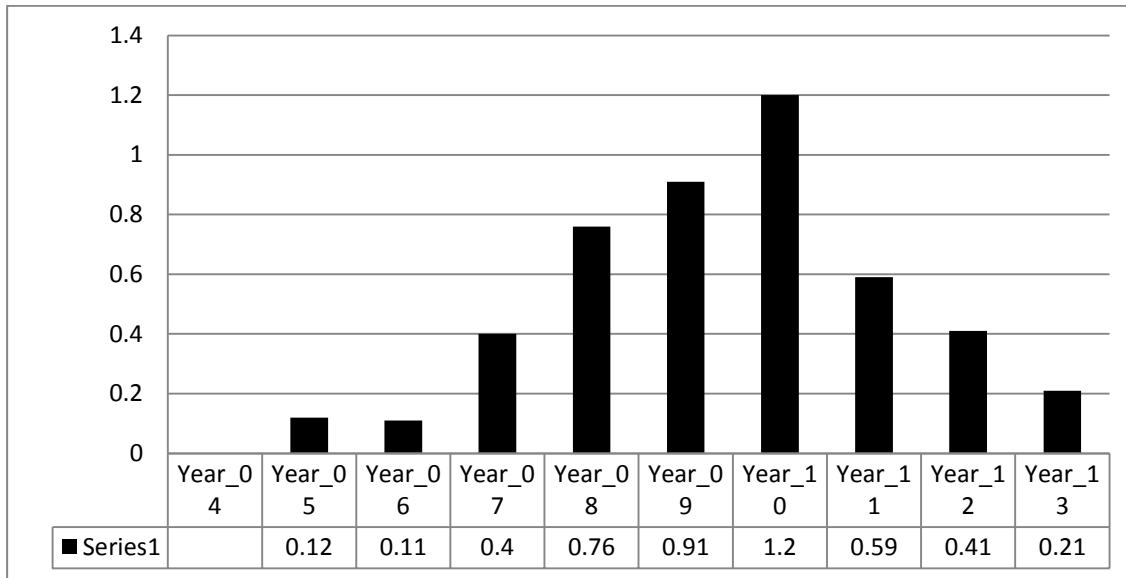


FIGURE 2: Weighted Figures of Higher Education Unemployment

The low community participation in higher education (HE) can occur because of a lot of possibilities, ranging from unaffordable costs, lack of public awareness of the importance of education for the future, and lack of belief that investment in education is something beneficial.

In West Java, the condition is not much different. People are more interested in having job as soon as possible in order to earn living, and ironically what society believe is evidenced by the data from West Java in Figure 2012 as shown in Figure 3.

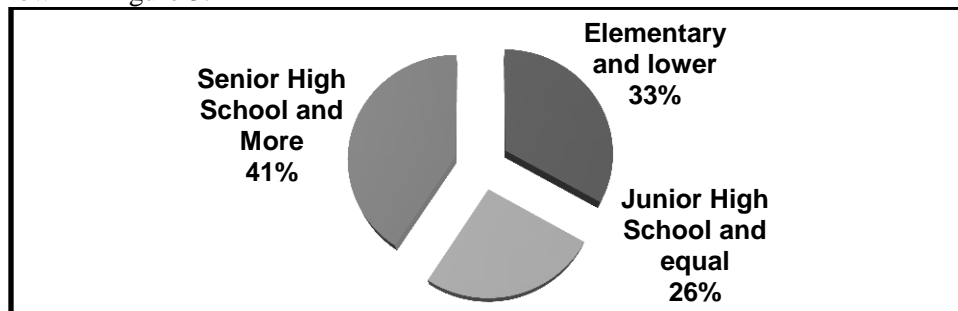


FIGURE 3: The Percentage of Unemployment by Education Level

When viewed from education level in West Java, the largest group of job seekers in 2012 came from the high school level of 54.35% followed by 38.49% of higher education and 5.53% of junior high school. While job seekers who had elementary education was only 1.63% (West Java in Figures 2012).

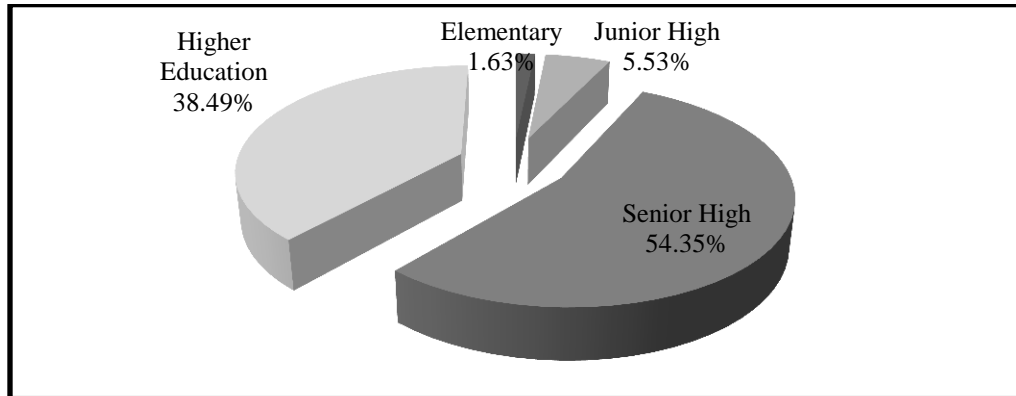


Figure 4: The Percentage of Job Seekers By Education Level in West Java in 2012

The Issues of the quality of university graduates get a lot of attention from various parties, one of which is from special staff of the Minister of Manpower and Transmigration, Abdul Wahid Maktub. Maktub stated that many colleges focused only on the pursuit of quantity of graduates without equipping them with skills (Antara News, 2013). The harder statement was stated by Vice President Boediono, "Colleges that do not keep the quality of their education like fake money dealers" (Metrotvnews, 2013). The inability of the college in maintaining the quality of education will result in declining the quality of graduates that will create the long-term damage to the system and affect the future of a nation.

The statement expressed by Maktub and Boediono is strengthened by the survey results of Times Higher World University on the university rankings based on teaching, research, knowledge transfer and international outlook. No Universities in Indonesia entered the ranks of Asia's best 60. This condition can be used as an indicator to see the quality of education in Indonesia, given that from South East Asia region, three Universities include in Asia's Best 60 namely National University of Singapore, Nanyang Technological University Singapore and King Mongkut's University of Technology Thonburi Thailand (times higher education, 2013).

The results of another study published by 4 International Colleges & Universities that arranged the top 100 Universities in Asia showed that only three Indonesian Universities, Bandung Institute of Technology (ITB), Padjadjaran University (Unpad) and Gajah Mada University (UGM) included in the ranking. Such numbers are still smaller than those in Thailand that include seven universities, Chiang Mai University, Burapha University, Kasetsart University, Prince of Songkla University, Mahidol University, Chulalongkorn University and King Mongkut's Institute of Technology Ladkrabang. Although Singapore and Malaysia included the smaller numbers of their universities, given the number of universities in Indonesia is far more, the condition is not something to be proud of.

These survey results show that other countries in ASEAN region like Thailand, Singapore, and Malaysia have better recognition in their higher education than Indonesia. Indonesia has far more colleges and universities but only three of them entered the best rank according to 4 International Colleges and Universities and no one include in the Asia's Best 60. The results also indicate the need for urgent efforts to improve the quality of education in Indonesia in order to produce quality graduates.

The increase of education quality in creating quality graduates can be accomplished if a university is able to create a sustainable atmosphere favorable to the creation of conducive institutional environment for the creation and improvement of education and graduates. This study focuses on two variables considered of having a role in creating this condition. The variables in question consist of the quality of Internal Audit and Good University Governance. The idea that such two variables are regarded as the contributing factors in the improvement of quality of HE operation can not be separated from the views of the researchers, governments, practitioners in the field of HE, and other parties who are concerned about improving the quality of education.

Internal audit existance as one of the variables considered to have contribution on the improvement of the quality of education that has the implication on the quality of graduates is based on the assumption that the



existence of internal audit quality in the institution will be able to create a control system of education operation as a form of professionalism in the college environment. This statement is as stated by Lustig (2006), 'Taken as a whole, what's distinctive about academic work over the centuries has been the high degree of professional autonomy required for its performance'.

Enhancing the quality of higher education that produces qualified graduates should always improve. What is distinctive about the academic work for centuries should be transformed into a high degree of professional autonomy necessary for a peak performance. In other words, the college activities should be transparent and accountable as it is conducted by profit organizations. The assumption is similar to that expressed by the Rector of the Islamic University of Indonesia Edy Suandi Hamid (Antaraneews, 2012): 'Internal audit can be used for the control and development of HE quality. Internal audit is a means to improve the performance of each unit in HE.'

Internal Audit is commitment and professionalism in universities in ensuring and improving the quality of education. Because of internal audit implementation, the university will be encouraged to be more transparent in demonstrating the performance achieved. Furthermore, the existence of the college consisting of work units require a tool to improve the quality of its education, so that they can show clearly to other related groups ways and methods to do evaluation and improvement in the future.

The existence of an internal audit is basically the implementation of the requirements of the standards prescribed by the National Accreditation Board of HE (BAN-PT). BAN-PT requires institutions to have financial, facilities, infrastructure and information management systems that ensure the feasibility, continuity, and sustainability of academic programs in study programs (Standard 6 of BAN-PT, 2011).

Internal audit quality will be the control instrument for the academic implementation processes in order that the process is implemented in an effective and efficient manner. This is due to related parties can have adequate access to the feasibility, quality and sustainability of the funding, infrastructure, facilities and information systems. Therefore, at the end the internal audit is able to improve the quality standards of excellence funding, facilities and infrastructure, as well as information systems capable of guaranteeing the quality of program and planned performance target (education, research and community service) (BAN-PT, 2011).

The second variable considered to contribute to the improvement of the quality of education and the quality of university graduates is good university governance. Good university governance is the example of standard and the approach used for quality control. It is very likely that an attempt to understand the quality of higher education can not be separated from the existence of good university governance. HE as one of the forms of organization, of course, will not separate themselves from efforts to maintain and improve its quality. The implementation of good university governance concept in HE will improve its quality in producing quality graduates, as stated by Corson in Indrajit (2006: 276) 'Governance is a decision-making process for making rules and regulation which govern the conduct of and relationship between the various member of the colleges or university community.'

Governance is the decision-making process in order to make rules and regulations that regulate the task execution of and the relationships among various members of the college or university. The efforts to improve the quality of higher education can be conducted by applying the principles of good governance, such as fairness, transparency, accountability, independence and responsibility. Through the implementation of university governance it will create university management that supports the improvement of the quality of higher education.

Based on the explanation, this research is directed to the central theme concisely formulated as follows: Up to now, the quality of HE operation and its graduates is still low. This can be seen from universities' inability in creating supportive atmosphere for the creation of an enabling institutional environment for the improvement of education operation and its graduates' quality on an ongoing basis. Therefore, it is necessary to take an effort to improve the quality of education operation and quality of university graduates, which is considered supported by the improvement of the quality of Good University Governance formed by internal audit quality.

In line with the central theme of the research, in an attempt to understand phenomena and solve the problem of low quality of HE and its graduates, it is necessary to do a research on models of these two variables by making the quality of Good University Governance established by the Internal Audit as an influencing variable.



2. Research Purposes

Based on the research background, the research problem can be formulated as follows:

- (1) How is the quality of university graduates in region III of West Java province.
- (2) How is the quality of HE operation in region III of West Java province.
- (3) How is the quality of internal audit in HE in region III of West Java province.
- (4) How is good university governance in region III of West Java province.
- (5) How is the effect of the quality of internal audit on good university governance and its implications on the quality of education operation that contribute to the quality of HE graduates in region III of West Java province.

LITERATURE REVIEW, CONCEPTUAL FRAMEWORK AND RESEARCH HYPOTHESIS

1. Literature Review

Graduates Quality

Literature review related to this endogenous variable begins by defining what the quality of graduates is. The quality of graduates stated by Indonesian Language Dictionary (KBBI), consists of two words, namely quality and graduates. Quality means "good or bad rate, grade, degree or level of something (intelligence, skills, and so on)". Quality basically is a measurement that differentiates rank, grade, degree or extent of the object assessed. Graduate means "to perform well or have succeeded in the face of all the trials (tests)". It means a graduate is a person who has completed a process with various tests intended as a determination of high and low ability in finishing the process.

Based on the KBBI definition it can be stated that the quality of college graduates means the degree of good or poor graduates who have completed a HE process measured from their intelligence or skill level and known from a series of tests that have been given as a guarantee for the accuracy of someone's high and low valuation. Furthermore, Kotler and Fox (1985 in Nicolescu: 2009) stated that 'Employers, too, benefit of the "results" of the higher education processes, as they use the skills and the abilities that graduates acquired during their studies.'

In Indonesia, the level of graduate quality is measured by their level of competence. Therefore, Indonesian government issued the competence-based learning curriculum or Competency Based Curriculum (CBC). Curriculum formation is closely linked to the curriculum objectives as a plan for the successful achievement of learning objectives (Unruh 1984 in Wijatno, 2009: 63). The meaning of competence, according to Minister of Education's Decree No. 045/U/2002 on core curriculum of college is a set of intelligent action and full responsibility owned by a person as a condition to be considered capable by the community in carrying out tasks in a particular job. This definition supports the notion of quality of graduates according to a statement previously described.

Referring to such opinions, it can be concluded that the notion of quality of graduates is the level of skill and ability individuals acquired during their studies, so that with such an attribute they are able to provide benefits to the organization where they stay. The quality of university graduate essentially is students who basically follow the process of education in the university that bring them to have useful science and knowledge at the end of the process. Students who follow the education process in a university is a consumer and the science and knowledge they acquire are product or outcome of the process of HE. Quality graduates are alumni who have science and useful knowledge and be able to apply these in their daily lives both in the social and working environment.

Based on such understanding, the researchers specify the measurement of the level of graduates quality by referring to BAN-PT that consists of three dimensions, namely:



1. Graduate profile, as measured by the timeliness of the study completion and students proportion.
2. Tracking and recording of graduate data measured based on the graduates' waiting period of their first work, the suitability of their field of study with their field work and the first working position.
3. Graduates' and alumni participation in supporting the academic and non-academic development of study program measured by their role in professional associations or the field of science and the mutual support of the alumni.

Quality of Higher Education Operation

The next literature review is to discuss the higher education, in which the definition is different from college. According to Indrajit (2006: 3), 'Higher education is education in school path which is higher than secondary education.' Indrajit further stated that college is an educational unit that organizes HE which is divided into Academy, Polytechnic, Colleges, Institutes, and Universities.

The quality HE operation produces the quality graduates (Indrajit, 2006). In other words, the quality of HE is a key in creating a qualified human resources who will be the successor of the nation development (Tambunan, 2008). The future of a nation will be determined by the extent of the success of educational institutions as a civilization factory of a nation in creating the qualified nation's generation. This is in line with Okwakol (2009), 'Higher education institutions are charged with formation of human capital through teaching, building knowledge base through research and knowledge development, and dissemination and use of knowledge by interacting with the knowledge users.'

In Indonesia, the HE management should hold three tasks of HE or *tri dharma perguruan tinggi* that consist of providing education, conducting research, and doing community service. This is regulated by Government Regulation No. 60/1990, the Education Law No. 20/2003 on National Education System and its implementation regulations that include the Indonesian Government Regulation No. 17/2010 on the Management and Operation of Education and Indonesian Government Regulation No. 66/2010 regarding the amendment of Government Regulation No. 17/2010 on the Management and Operation of Education.

National education system is currently regulated by Law No. 20/2003 on National Education System. National education system is the whole educational components correlated in an integrated manner to achieve national education goals. National education is education that is based on Pancasila and 1945 Constitution rooted from religious values, Indonesian national culture and the response to the demands of the changing times. The function of national education is to develop the ability and to form the dignified character and civilization of the nation in order to achieve the intelligent life of the nation. National education goal is to develop the potential of students to become a man of faith and fear of God Almighty and to be noble, healthy, knowledgeable, skilled, creative, independent, democratic and responsible citizens. To embody such missions, HEs have a task to do *tridharma perguruan tinggi*.

In terms of measuring the level of quality of HE operation, all parties in Indonesia should refer to BAN-PT as the agency responsible for controlling the quality of HE operation in Indonesia. BAN-PT establishes the measures to determine the quality of HE that consist of four dimensions, namely:

1. Lecturers' quality measured by their academic qualifications and reputation, the breadth of their networking in academic and professional, and their expertise in accordance with the needs.
2. Research quality measured by the lecturers' researches that get awards and grants and the clarity of research management system.
3. Internal Process in serving students measured by lecturers' workspace, access to facilities, and utilization of facilities.
4. Innovations of study program measured by the involvement of study programs in the improvement of learning strategies and techniques and viewed from efforts in improving lecture activities.

Good University Governance

There are five basic principles of good corporate governance (GCG) including transparency, accountability, responsibility, independency and fairness (Daniri, 2005). Transparency can be interpreted as



information disclosure, both in the decision-making process and in revealing relevant material information regarding the company. In realizing transparency, the company must provide sufficient, accurate and timely information to various interested parties. If the principles of transparency are properly implemented, conflicts of interest among various parties in the management are very likely to be avoided.

The essence of GCG includes both corporate performance improvement through supervision or management performance monitoring and management accountability to other stakeholders, based on a framework of applied rules and regulations (Gunarsih, 2003). GCG provides a frame of reference that allows monitoring mechanism to run effectively so as to create checks and balance mechanism in the company.

In a simple way, GCG in HE can be viewed as the application of basic principles of good governance concept in the system and process of governance in HE institutions, through various adjustments made based on the values that must be upheld in the operation of HE in particular and education in general (Wijatno, 2009). Adjustment in the application of Good University Governance (GUG) is because the higher education is expected to be able to produce innovations and ideas in dealing with the problems facing the nation. In addition, HE is also regarded as a guard for moral and noble values held by a nation, including culture, customs, habits and so on. With a large role and expectation, the HE community gets a respectable position in the society.

In Australia the study conducted by the Higher Education Management Review Committee-Hoare (2001 cited in Wijatno 2009) has identified that a lack of adequate skill and understanding of the HE sector has been the cause of performance problems in university management. This problem is partly due to the weakness of the university manager selection process and the lack of training for university managers. Therefore, the Australian government adopted a policy on the university management that has major influence over universities through university funding agreement requirements. The policy is the implementation of the National Governance Protocols (NGP) in Higher Education Support Act. Under these rules, the universities in Australia have obligations to:

1. Set up institutional goals, tasks and obligations of the university management institutions.
2. Implement the professional development and performance appraisal program of university management institutions.
3. Establish procedures for members election of the management institutions, including specification and expertise requirement.
4. Codificate and report business practices at the university.

The NGP has led to several follow-ups, including the adjustments of internal rules of each university in accordance with the concept, theory and practice of good governance in the HE sector in Australia. Three factors contribute to the rapid development of university management in Australia:

1. High attention on the impact of increasing entrepreneurial and commercial activities undertaken by the university.
2. Attention on some inappropriate roles, i.e. some university leaders act without sufficient responsibility, or the existing of administrator intervention on the executive policy.
3. Broader development of corporate governance, including some new guideline issues published by the Australian Stock Exchange.

Various experiences in several countries suggest that universities have distinctive characters with the company in general. However, there are some fundamental similarities that is management and accountability to stakeholders. Therefore, the application of good governance in HE should be adapted with the specific characteristics of the university.

One of the GUG implementation steps is conducting performance improvement through restructuring. Restructuring can be implemented in various ways by among others improving financial performance, giving broad powers to the management in carrying out its functions and the reduction of bureaucracy. Giving broad authority to the management in decision making is an effort to improve the performance of HE. This is in line with the concept of a new paradigm in HE that puts four important aspects: autonomy, accountability, accreditation and evaluation (Higher Education General Directorate, 2002 in Wijatno, 2009: 133).

The HE management should be able to proper implement an adaptation process. In addition, the management should be responsible for controlling the organization so that the vision and mission of HE can be



achieved as expected. The mission of HE in accordance with Tri Dharma Perguruan Tinggi revolves around implementing education and teaching, research and community service. Along with the development of the era and the influence of globalization, HE is demanded not only operating the mission but also conducting quality assurance (QA). Although QA is not widely known by the HE managers and has not been a culture, QA is very important to be used as a reference in order to improve the quality and performance. Society as a source of HE funding is entitled to obtain information about the HE's performance (Higher Education General Directorate, 2002 in Wijatno, 2009: 133).

Internal Audit

The implementation of internal audit at this time is not only applied in the business activities but has begun to be applied in HE operations. The internal audit has a purpose to improve the effectiveness and efficiency of HES in their operational activities.

Internal Audit, commonly called Internal Audit Unit (SPI), according to the Internal Audit Profession Standards (2004) is defined as:

"Assurance and consulting activity which is independent, objective and designed to add value and to improve organization's operations. Internal audit helps the organization achieve its objectives, through a systematic and orderly approach to evaluate and improve the effectiveness of risk management, control and governance processes."

Agoes (2004: 221) defines internal audit as:

"Verifications carried out by the company's internal audit body against the company's financial statements, accounting records and compliance on top management policies that have been defined, government regulations and the provisions from applicable professional associations."

From both definitions, it can be summarized that the internal audit activity is not only limited in the field of financial audit but already includes consultation designed to add value and improve organization's operations. To achieve these objectives, the internal auditor should perform the following activities:

1. Reviewing and assessing goodness, adequacy and application of management control systems, internal control and other operational control and developing effective control at a reasonable cost.
2. Ensuring adherence to policies, plans and procedures established by management.
3. Ensuring how much company's property is accounted for and protected from the possibility of any form of theft, fraud and abuse.
4. Ensuring that the management of data developed within the organization can be trusted.
5. Assessing the quality of each piece of work in carrying out the tasks assigned by the management.
6. Suggesting operational improvements in order to increase efficiency and effectiveness.

Internal auditors are required to always develop knowledge, skills and discipline in their work. International Standards for the Professional Practice of Internal Auditing (IIA, 2009: 9) mention that "engagement should be performed with proficiency and due professional care". This is further elaborated as follows:

1. Proficiency. Internal auditors must have knowledge, skills, and competencies required to carry out responsibility individually. Collectively, internal auditors should have knowledge, skills, competencies necessary to perform their responsibilities including:
 - The chief audit executive should obtain competent advice and assistance if the internal staff lacks the knowledge, skills, or other competencies needed to perform all or part of the engagement.
 - The internal auditors should have sufficient knowledge to identify the indicators of fraud but it is not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.
 - The internal auditors should have knowledge of key information technology risks and controls and available technology-based audit techniques to perform their assigned work. However, not all internal auditors are expected to have the expertise of an internal auditors whose primary responsibility is information technology auditing.



2. Due Professional Care. Internal auditors must apply care and skill in doing their job as expected. In applying their professional rigor, internal audit needs to consider the following matters (IIA, 2004: 9-10):
 - Extent of work needed to achieve the engagement's objective.
 - Relative complexity, materiality, or significance of matters to which assurance procedures are applied.
 - Adequacy and effectiveness of risk management, control, and governance processes.
 - Cost of assurance in relation to potential benefits.

3. Quality Assurance and Improvement Program

Person in charge of the internal audit function should develop and maintain a program of quality assurance and improvement covering all aspects of internal audit function and continuously monitor its effectiveness. This program is designed to help internal audit to add value, improve organization's operations and provide assurance that the internal audit function has been in accordance with the standards and code of conduct of internal audit.

2. Conceptual Framework

Based on the literature review, some described studies and followed by an elaboration of research framework in explaining how the relationship among research constructs and their theoretical argument, this research topic emerges. The quality of HE and graduates is the output and at the same time the goal of an institution of HE. In other words, both constructs are the form of the effectiveness of the university as a type of HE institution. Organizational effectiveness is measured by to what extent has the organization fulfilled its goals and objectives and how well this is conducted in the process (Yankey and McClellan, 2003; in Kronkosky, 2007).

The conceptual framework of this study uses the theory of Competing Value Approach proposed by Robert E. Quinn and John Rohrbaugh (1983: 363-377). This theory is a new and the most advanced approach in the study of organizational effectiveness (Robbins, 1994; Rollinson and Broadfield, 2002). Furthermore, Kusnendi (2006) said:

"The effectiveness of the organization in terms of the conceptual model of competing values is not only seen from the perspective of objective optimization and system framework, but also viewed in the perspective of strategic constituencies. Thus, basically competing value model is a combination or integration of three models of organizational effectiveness study that developed earlier."

The choosing of competing values approach theory in the conceptual framework is used to explain the relationship among such constructs. Referring to the understanding of both constructs as exogenous variables or in competing values concepts known as input factors (in this research are internal audit and GUG), it is believed that both can contribute to the quality of HE operation and quality of graduates.

Internal Audit and GUG reflect the effort to achieve effectiveness in a different angle. Internal audit is the form of effectiveness derived from a goal attainment approach while GUG is a form of achievement of the effectiveness from the open system approach. The form of effectiveness achievement is based in the strategic constituency approach. The incorporation of these three constructs showed competing values models of a university.

Referring to the theory of competing values model this research obtained four premises that will be the foundation of reasoning in formulating research hypotheses.

1. Quality HE operation and university graduates can be achieved with the implementation of internal audit as an application of internal process model that ensures the information condition and stability of the objective achievement effectively and efficiently. This approach holds that, the organization is the entity established deliberately and rationally and has a definite purpose. Therefore, according to this approach, the effectiveness of an organization has to be seen from the criteria of how the organization is able to achieve the goals that have been set forth. According to Steers (1985 in Kusnendi, 2006), the proponents of the goal achievement approach has given rise to univariation criteria in measuring the effectiveness of the organization. Steers (1985, in Kusnendi 2006), based on meta analysis of several studies conducted by experts during the period of 1960s, successfully identified nineteen measures of organizational effectiveness. From nineteen measures, the four most widely used are profitability, productivity, efficiency,

and rate of employee's turnover (Steers, 1985 in Kusnendi, 2006). Internal process by implementing the internal audit is an attempt to perform an adequate control or supervision on the organization activities, in order to achieve HE effective management as well as economically efficient (Wijatno, 2009: 227).

2. GUG is the application of the rational goal model in creating productive and efficient HE institutions. Rational goal model achievement can be done with GUG. GUG is basically applied to build confidence in attracting foreign investors to do investment, and foreign investors in the education world is the government and the international community (Serian, 2009: 128). Strategic constituency approach, or often referred to as the multiple constituency model of effectiveness (Gibson, Ivancevich & Donnelly, 1996: 45) views the organization as a political arena where interest groups compete for control of resources (Robbins, 1994: 69). Therefore, this approach considers that the organization is effective if it is able to meet the demands of the constituency or stakeholders that are present in the organization's environment, especially the stakeholders that predominantly affects the continuity of the organization (Kreitner & Kinicki, 2001: 633-634).

Based on a literature review and some research results as already described, the following is proposed research framework. To explain how the patterns of relationships among constructs studied and its theoretical arguments, this study used the conceptual framework of organizational behavior.

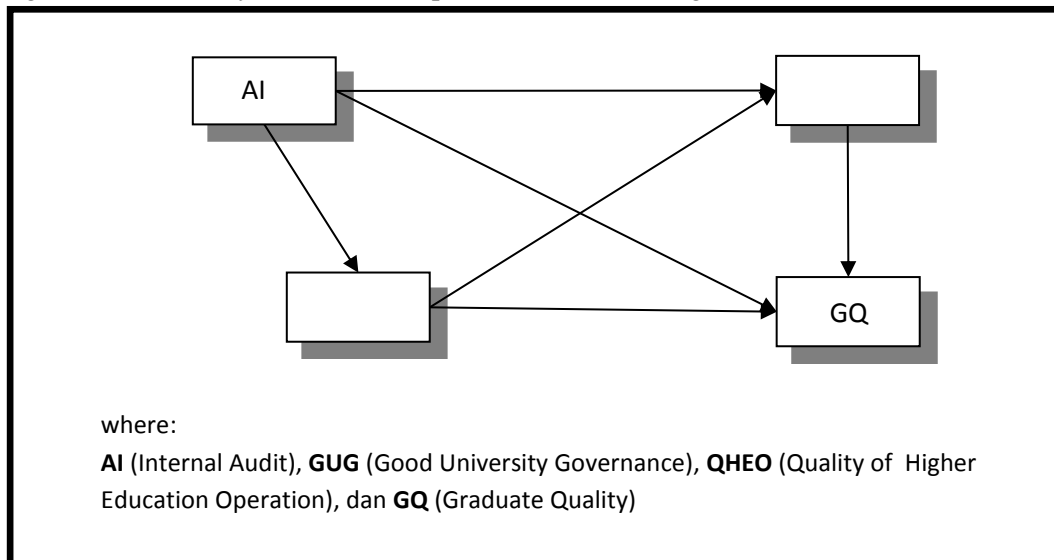


FIGURE 5: Thinking Framework of Model of of Higher Education Operation Quality and Graduate Quality

Figure 5 is a model proposed in the study based on a literature review and thinking framework. This is the model of enhancing the quality of HE and the quality of graduates that has two sub-models:

1. **GUG Model**

$$GUG = f(IA) + e^1$$

2. **QHEO Model**

$$QHEO = f(IA, GUG) + e^2$$

3. **GQ Model**

$$GQ = f(IA, GUG, QHEO) + e^3$$

Where:

IA = Internal Audit

GUG = Good University Governance.

QHEO = Quality of Higher Education Operation.

GQ = Graduate Quality.



4. Research Hypothesis

Based on the problem formulation, framework and premise, the research proposes hypotheses and sub-hypotheses

Hypothesis

The quality of internal audit affects Good University Governance, and it has an implication on the quality HE operation that contributes to the quality of HE graduates in region III of West Java province.

Sub Hypothesis.

Sub hypothesis of the study is conducted with viewing the number of sub-models in the study. The sub-hypotheses include:

First Sub-hypothesis

Internal Audit affects Good University Governance.

Second Sub-hypothesis

Internal Audit and Good University Governance affects the quality of higher education operation.

Third Sub-hypothesis

Internal Audit, Good University Governance and the quality of higher education effects the quality of graduates.

RESEARCH METHODS

This study was designed to explore the measurement process of internal audit quality against GUG and its implications on various variables that theoretically have contribution on or affect the quality of HE. Exploration of the exogenous variables is the first step to identify the strength of various variables' effects on the measurement of HE quality.

The population of this study is the head of the private university study programs in region III of West Java province consisting of Cirebon City and Cirebon, Indramayu, Majalengka, and Kuningan Regency. The sampling technique used is saturated sampling, where all members of the population become the study sample (Mahadianto & Setiawan, 2013). Of the 99 questionnaires distributed only 65 questionnaires were declared eligible for further estimated, determined from the completeness of the respondents in filling out the questionnaires.

The testing of validity (standard > 0.3) and reliability (standard > 0.7) uses Cronbach's Alpha for each instrument spread out started from the testing results of validity and reliability of Internal Audit, GUG, the quality of HE operation and the quality of graduates. Only one question of the quality of HE is declared invalid, while the entire questionnaires have no problem with reliability values.

The statistical analysis in this study uses descriptive statistics and inferential analysis. The use of both types of statistics can not be separated from research goal-setting. Descriptive statistics analysis is used to get an idea of the existence or execution of the variables studied while inferential analysis is used to analyze the influence of exogenous on endogenous variables (Mahadianto & Setiawan, 2013). Descriptive analysis was conducted by calculating the mean value, while inferential analysis used path analysis.

The interpretation of the score is conducted by taking into account the empirical mean score (X), the theoretical average score (μ) and theoretical standard deviation score (σ). The categorizing is concentrated based on three levels: high, medium and low.



TABLE 1: Categorization of Variable Level

Scale Score			Score σ	Score μ	Score Range	Category
Min	Max	Range				
1	5	4	0.67	3	1.00 – 2.32	Low
					2.33 – 3.67	Medium
					3.68 – 5.00	High

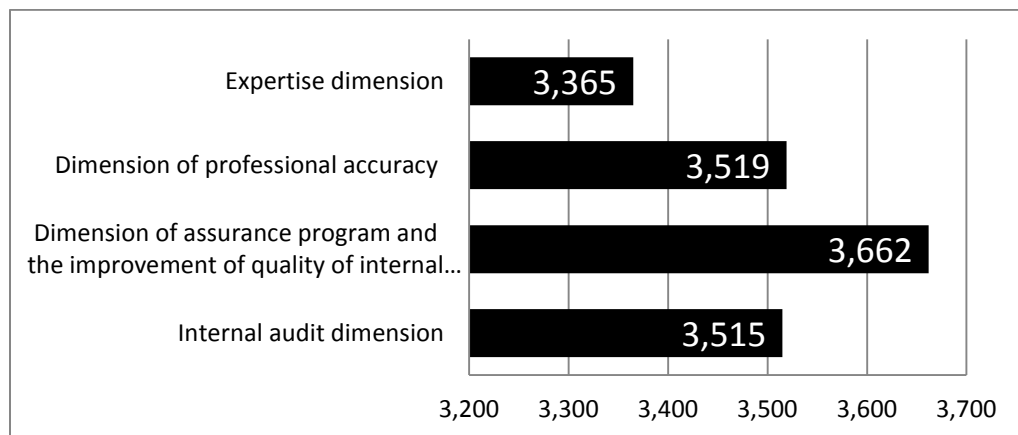
RESEARCH RESULTS AND DISCUSSION

1. Validity Analysis

Research result was obtained from questionnaires distributed to universities in region III of West Java consisting of Cirebon City and Cirebon, Indramayu, Majalengka, and Kuningan Regency. Of the 99 questionnaires distributed only 65 questionnaires were completed by respondents. Furthermore, the validity and reliability testing was conducted to determine the degree of data validity from questionnaires distributed.

2. Descriptive Analysis

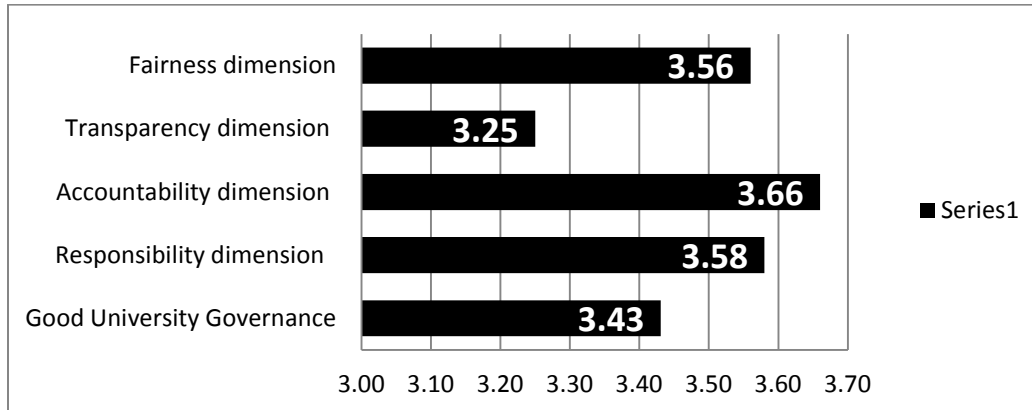
Descriptive analysis was conducted to see the implementation of internal audit, GUG and the quality of HE in private universities under study. The first is related to the analysis of the internal audit which is built by three dimensions. Based on the descriptive statistical analysis by estimating the mean score, the respondents' responses are as shown in Figure 7.



Source : Data Pocessed 2014

FIGURE 7: Mean Values of Internal Audit Dimension

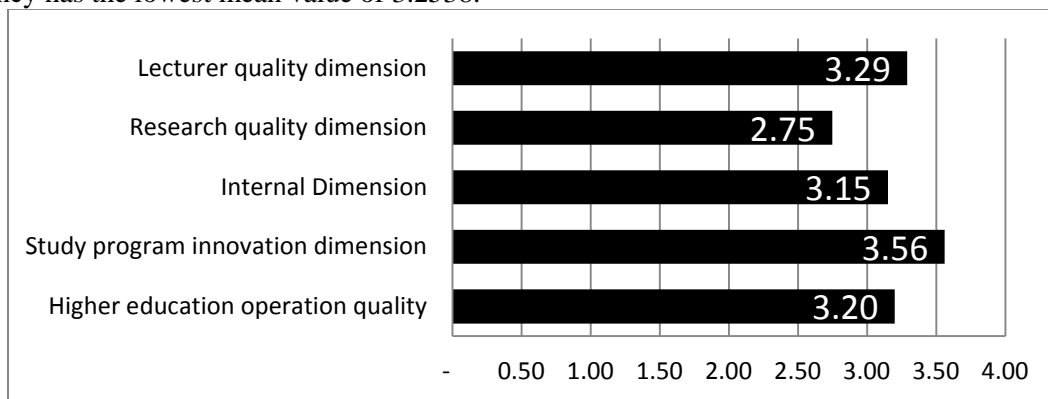
Based on the descriptive analysis it is known that the internal audit of private universities in Region III is in the criteria of Sufficient with mean value of 3.515 (2.33 to 3.67). Of the three dimensions of internal audit quality, expertise has the lowest mean value of 3.365 (2.33 to 3.67). This value indicates that the quality of internal audit in the private universities in Region III of West Java Province has not been as expected.



Source: Data Processed 2014

FIGURE 8: Mean Value of Good University Governance Dimension

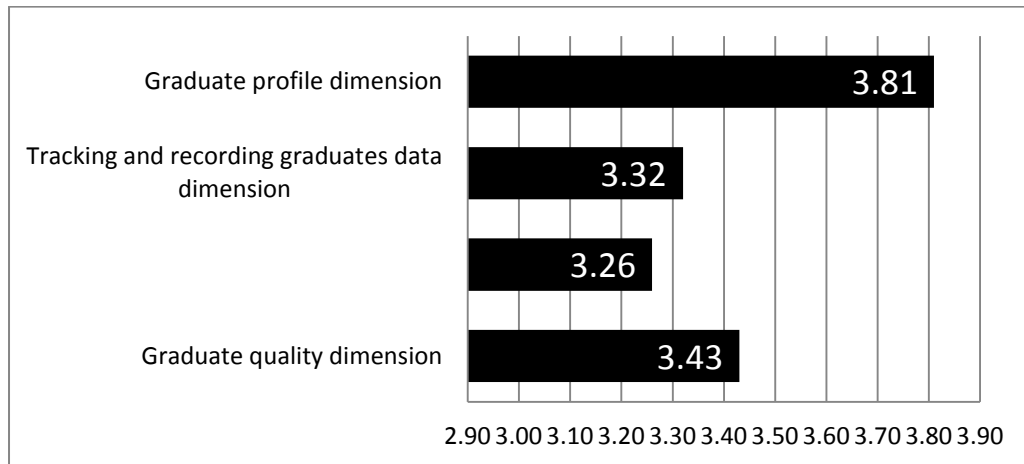
Based on the descriptive analysis it is known that GUG in private universities in Region III is in the criteria of Medium with the mean value of 3.4308 (2.33 to 3.67). Of the four GUG dimensions it is known that dimension of transparency has the lowest mean value of 3.2538.



Source: Data Processed 2014

FIGURE 9: Mean Value of Quality of Higher Education Operation Dimension

Based on the descriptive analysis it is known that the quality of HE operation is in the criteria of Sufficient. HE quality is seen from the mean value of lecturer quality dimension of 3.201275 (2.33 to 3.67). From the four qualities of HE operation, it is known that the mean value of the research dimension is the lowest compared to other dimensions with the average value of 2.7949.



Sources: Data Processed 2014

FIGURE 10: Mean Value of Graduate Quality Dimensions

Based on the descriptive analysis it is known that the quality of graduates is in the Sufficient criteria with the value of 3.4391. Of the three dimensions it is known that the mean value of graduates and alumni participation in supporting the development of academic and non-academic study program shows the lowest value of 3.2654 (2.33 to 3.67).

3. Path Analysis

The analysis carried out to achieve the goal of the research is path analysis with AMOS as a tool to help the estimation. In this inferential analysis, the data collected from questionnaires will be estimated to determine the level of significant influence of the internal audit and GUG on the quality of HE operation both simultaneously and partially. Furthermore, the effect decomposition of each variable will also be estimated.

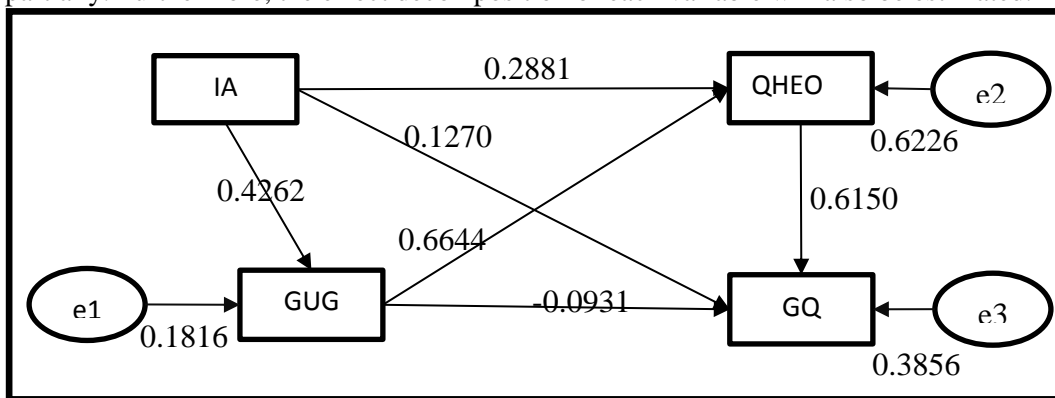


FIGURE 11: Path Analysis of Quality of HE Operation and Graduates Quality

The estimation results of the path model proposed in accordance with the literature review and thinking framework produce several paths that have no significant value. With 1% error level (0.01) it is known that there is insignificant effect between the IA and QHEO ascertained from the value of C.R. 2.687 with significant value of 0.007. Furthermore, there is a path between GQ and IA indicated from the value of C.R. 1.112 with significant value of 0.266. And the last is between GUG and GQ with C.R. value of -0.615 with a significant value of 0.539.

TABLE 2: Partial Hypothesis Testing

	Estimate	S.E.	C.R.	P	Label
GUG <--- IA	.968	.257	3.769	***	par_3
QHEO <--- GUG	.283	.036	7.826	***	par_1



	Estimate	S.E.	C.R.	P	Label
QHEO <--- IA	.221	.082	2.687	.007	par_4
GQ <--- QHEO	.427	.111	3.856	***	par_2
GQ <--- IA	.085	.077	1.112	.266	par_5
GQ <--- GUG	-.028	.045	-.615	.539	par_6

The insignificant path values has made the proposed model become Non-Fit. In other words, the proposed model can only be applied to the sample only, and can not be generalized into the whole population. Therefore, the researcher attempted to improve the proposed model in order to obtain a model that can be generalized into the whole population. Following the improvement, a new and more parsimonious model in describing the causality relationship among variables studied were achieved.

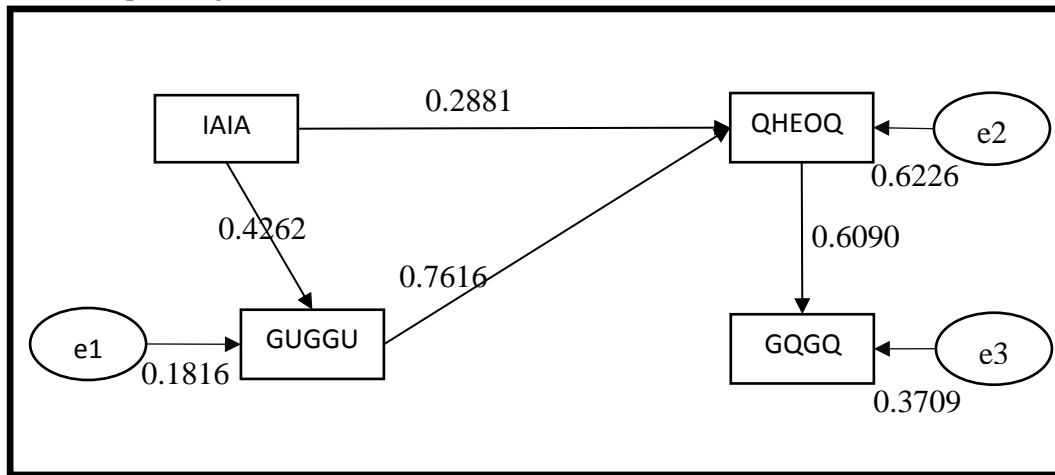


FIGURE 12: Model after being Improved

The model that has been improved can be interpreted as a fit model indicated from testing result of Good Fit Index as shown in the table.

TABLE 3: Fit Model Test

GFT Size	Criteria of Model Fit	Testing Criteria	Implication on Ho	Decision
Chi-Square	0.450	≥ 0.05	Accepted	Model Fit
RMSEA	0.000	≤ 0.08	Accepted	Model Fit
GFI	0.988	≥ 0.90	Accepted	Model Fit
AGFI	0.942	≥ 0.90	Accepted	Model Fit
NFI	0.986	≥ 0.90	Accepted	Model Fit
TLI	0.999	≥ 0.90	Accepted	Model Fit
CFI	0.991	≥ 0.90	Accepted	Model Fit

Test results of overall model fit against the improved model provide goodness of fit with the size or index that gives RMSEA value smaller than 0.08, and the values of GFI, NFI, TLI and CFI are all greater than the limit value of the model fit (≥ 0, 90). Good of fit value indicates that the model that has been improved is a fit model. Besides, the improved models are more parsimonious than the proposed model.

Based on the results of these tests it is found that the implementation of Internal Audit in private universities in region III of West Java affects Good University Governance. In addition, GUG and internal audit contribute to quality of HE operation which ultimately has implications on the quality of university graduates.



Based on the path coefficient value it is known that good university governance has dominant influence on the quality of HE operation compared to internal audit. The analysis also shows that the quality of HE operation has significant influence on the quality of graduates produced.

CONCLUSION AND RECOMMENDATION

1. Conclusion

The conclusions of the research on the contribution of Internal Audit and Good University Governance on the Quality of Higher Education Operation, and its implications on the quality of university graduates in Private universities in region III West Java province are as follow:

- (1) The quality of graduates from private universities in region III of West Java province is on the criteria of Medium. The most prominent issue is the participation of graduates or alumni in supporting the academic and non-academic development of study program.
- (2) Based on the descriptive analysis it is known that the level of quality of HE operation is in the Medium category. The lowest indicator is related to the quality of research that still need further improvement.
- (3) The level of internal audit quality in private universities in the Region III of West Java is still in the Medium category. The lowest indicators is in the category of Expertise possessed by the internal auditors.
- (4) The results of descriptive analysis indicate that Good Universtiy Governance at private universities in Region III of West Java is in the Medium category. The lowest indicator is on level of Transparency in governance activities.
- (5) The results of inferential analisis indicate that internal audit has a significant effect on the establishment of private universities' governance in Region III of West Java province.
- (6) The analysis results indicate that the level of Internal Audit quality and Good University Governance affect the quality of HE operation in private universities in Region III of West Java.
- (7) Based on the second sub-models that have been improved only the quality of HE operation that directly affects the quality of graduates. The Internal Audit and GUG gives only an indirect effect through the quality of graduates in Private Universities in Region III of West Java.

2. Recommendation

Based on the findings of the study on the effect of Internal Audit and GUG on the Quality of HE operation and its implications on the quality of university graduates in Private universities in Region III West Java, the research suggests:

- (1) The improvement of the quality of graduates through the participation activities of the graduates or alumni in supporting the academic and non-academic development of study program should be developed. This is because the alumni or graduates can be considered as service users of the universities. They know the shortcomings of their educational activities and things that should be improved in order to improve the quality of graduates.
- (2) The improvement of the quality of HE operation is absolutely necessary. One thing that should be conducted as soon as possible is the improvement of the research quality. Quality research is the scientific research that can produce and develop information and knowledge. Quality research will also encourage better development of environmental science at the private universities under study.
- (3) The improvement of the quality of internal audit at private universities in the area of study must be improved with among others improving the skills and capacity of the internal audit. Such efforts can be made by improving the knowledge, skills and competence of the internal auditors.
- (4) GUG in private universities in Region III of West Java should be improved by increasing the transparency of governance. Such transparency improvement can be done by increasing the ease of obtaining information about policy, program activities and financial statements.



- (5) As a model this research can function as guidance showing that in order to improve the quality of graduates, private universities in Region III of West Java should begin with improving the quality of their internal audit and GUG. Paying attention to these two factors is believed to be able to create quality HE operation that leads to improved quality of graduates.

References

- Agoes, S. (2004). *Auditing*. Jakarta: Salemba Empat.
- Arens, A. A. (2006). *Auditing dan Pelayanan Verifikasi*. Trans: Ford Lumban Gaol. Ninth Edition. Jakarta: Indeks.
- Azwar, S. (2008). *Penyusunan Skala Psikologi*. Yogyakarta: Penerbit Putra Pelajar.
- Badan Akreditasi Nasional Perguruan Tinggi (2008). Akreditasi Program Studi Sarjana Buku 2 Standar dan Prosedur Akreditasi. Retrieved from <http://ban-pt.kemdikbud.go.id/bb10/S1/BUKU%201-NASKAH%20AKADEMIK%20AKREDITASI%20PROGRAM%20STUDI%20SARJANA.doc>.
- Boynton, J. D. (2003). *Modern Auditing*. Trans: Paul A. Rajoe. Seventh Edition. Jakarta: Erlangga.
- Budiansyah, Y. (2011). *Pengaruh Kompetensi Dosen, Komitmen Organisasional, Motivasi Kerja Dosen, dan Budaya Organisasi terhadap Kinerja Dosen dan implikasinya terhadap Efektivitas Organisasi pada Universitas Swasta di Kota Bandung*. Unpublished Master Thesis, Padjadjaran University, Bandung.
- Burhani, R. (2012 July, 27). Rektor UII: Audit Internal Diperlukan Perguruan Tinggi. Antrara News. Retrieved from <http://www.antaraneews.com/berita/324041/rektor-iii-audit-internal-diperlukan-perguruan-tinggi>.
- Central Bureau of Statistic (2012). *Angka Partisipasi Murni (APM) menurut Tipe Daerah, Jenis Kelamin dan Jenjang Pendidikan, 2009-2012*. Retrieved from http://www.bps.go.id/tab_sub/view.php?tabel=1&daftar=1&id_subyek=40¬ab=14.
- Daniri, M. A. (2005). *Good Corporate Governance*. Jakarta: PT. Ray Indonesia.
- Gunarsih, Tri. (2003). *Struktur Kepemilikan Sebagai Salah Satu Mekanisme Corporate Governance*, kompak nomor 8 .
- Hakim, L. (2013, October 7). Kemenakertrans: Perguruan Tinggi Masih Berorientasi Kuantitas Lulusan. *Antara Yoga*. Retrieved from <http://www.antarayogya.com/berita/316218/kemenakertrans-perguruan-tinggi-masih-berorientasi-kuantitas-lulusan>.
- Indrajit, E. R.dan Djokropranoto. (2006). *Manajemen Perguruan Tinggi Modern*. Yogyakarta : CV. Andi Offset.
- Internal, K. O. (2004). *Standar Profesi Audit Internal*. Jakarta: Yayasan Pendidikan Internal Audit.
- Keasey, K. D. (1997). *Corporate Governance Responsibilities, Risks and Remuneration*. England: John Wiley & Sons Ltd.
- Kronkosky Charitable Foundation. (2007). *Non Profit Organizational Effectiveness*. Retrieved from http://www.kronkosky.org/research/Research_Briefs/Nonprofit%20Organizational%20Effectiveness%20January%202007.pdf.



- Kusnendi. (2006). *Pengaruh Kompetensi, Komitmen dan Budaya Organisasi terhadap Aktualisasi Peran Manajer serta Efektivitas Organisasi (Survei pada Industri jasa BPR di Wilayah Kerja Kantor Bank Indonesia Bandung)*. Unpublished Dissertation, Padjadjaran University, Bandung.
- Kusnendi, & Suryadi, E. (2010). *Analisis Jalur Dengan Amos*. Bandung: Rizqi Press.
- Lustig, J. (2006). From Art to Alienated Labor: The Degradation of Academic Work. *The Nea Higher Education*. Retrieved from www.nea.org/assets/img/PubThoughtAndAction/TAA_06_14.pdf.
- Mahadianto, M. Y., & Setiawan, A. (2013). *Analisis Parametrik Depedensi dengan Program SPSS (untuk pengolahan data tugas akhir, skripsi dan tesis)*. Jakarta: Rajawali Press.
- Nicolescu, L. (2009). Applying Marketing To Higher Education. *Scope And Limits Management & Marketing*, 4, No. 2, 35-44.
- Okwakol M.J.N. (2009) The Need for Transformative Strategic Planning in Universities in Uganda. *NCHE Journal Kampala*.
- Robbins, S. P. (1994). *Teori Organisasi Struktur, Desain dan Aplikasi*. San Diego: Prentice-Hall International, Inc.
- Robert E. Quinn, & Rohrbaugh, J. (1983). A Spatial Model of Effectiveness Criteria: Towards A Competing Values Approach To Organizational Analysis. *Jurnal Management Science*, 29 No. 3, 363-377.
- Rollinson, D., & Broadfield, A. (2002). *Organisational Behaviour and Analysis: An Integrated Approach*. Harlow: Financial Times Prentice Hall.
- Suhendi (2012). *Perancangan Sistem Pengukuran Kinerja MB-IPB Dengan Metode Balanced Scorecard*. Unpublished Master thesis, Institut Pertanian Bogor, Bogor.
- Tambunan, T. (2008). *Ukuran Daya Saing Koperasi Dan UKM*. Pusat Studi Industri dan UKM, Universitas Trisakti: Kadin Indonesia.
- Times Higher Education (s.a.). *World University Rankings 2013-2014*. Retrieved from <http://www.timeshighereducation.co.uk/world-university-rankings/2013-14/world-ranking/region/asia/range/001-200/order/rank|desc>.
- Utami, P. B. (2013, September 03). Lulusan tidak Bermutu, Perguruan Tinggi Ibarat Pengedar Uang Palsu. *Metro TV News*. Retrieved from www.metrotvnews.com/metronews/read/2013/09/03/1/179181/Lulusan-tidak-Bermutu-Perguruan-Tinggi-Ibarat-Pengedar-Uang-Palsu.
- Wijatno, S. (2009). *Pengelolaan Perguruan Tinggi Secara Efisien, Efektif dan Ekonomis*. Jakarta: Salemba Empat.
- 4 International College and University (s.a.) *Top 100 Universities and Colleges in Asia*. Retrieved from <http://www.4icu.org/topAsia/>.



The Effect of General Allocation Fund (DAU) and Regional Real Income (PAD) on the Regional Expenditures (Empirical Studies of the Government District/city of the Province of Bengkulu)

By

Nila Aprila ¹⁾

ABSTRACT

This research is empirical studies. This study aims to determine the influence of the General Allocation Fund (DAU) and Regional Real Income (PAD) on the Regional Expenditures (BD) of the district/city of the province of Bengkulu. Data used in this study is the Regional Financial data 2004 until 2009. Data were analyzed by SPSS version 16. From the data processing, it is known that the General Allocation Fund (DAU) has a positive and significant influence on Regional Expenditure (BD) in 6 districts/cities in the province of Bengkulu. While source Regional Real Income (PAD) has a positive and not significant to the Local Expenditure (BD) in 6 districts/cities in the province of Bengkulu. From the results of analysis the influence of the General Allocation Fund (DAU) and Regional Real Income (PAD) of Regional Expenditure (BD) is obtained that has occurred the flypaper effect, whereby Regional Expenditure (BD) are more dominated by the General Allocation Fund (DAU) than the amount of Regional Real Income (PAD).

Keywords: *General Allocation Fund, Regional Real Income, Regional Expenditures, Flypaper Effect.*

1) Economic and Business Faculty of University Bengkulu

INTRODUCTION

Background

Regional autonomy policy change in Indonesian regional government functions from centralized to decentralized. Centralization is a government policy that is managed by the central government and local governments throughout the policy determined by the central government. This tends to cause relatively greater costs in the management of local government, where the use of state finance becomes less efficient. So the central government issued a policy which authorizes each county in managing and regulating all the affairs of local government. The policy is regional autonomy and fiscal decentralization, where the policy is regulated in Law Number 32 Year 2004 on Regional Government and Law No. 33 of 2004 on Financial Balance between Central and Local Government. The implementation of regional autonomy and fiscal decentralization in Indonesia brought many significant changes. Experience in other countries shows that to achieve broad regional autonomy, real, and responsible takes a relatively long



time and requires consistency and effort policy of continuous improvement. The transfer of most government affairs followed by fiscal decentralization, in recent years Indonesia has been implementing political decentralization, which among others is realized with the direct regional elections. In addition to decentralization of political, economic decentralization is manifested also by giving freedom to the region to carry out development in accordance with the potential, conditions, and characteristics of the area (Ministry of Finance of the Republic of Indonesia, 2010).

Authorizing the use of all the fund balance has been left entirely to local governments. However, local governments have to use effectively and efficiently in order to improve standards of public service and is presented in a transparent and accountable. But in practice, the central government transfers are often used as the main source of funding by local governments to finance day-to-day operation of the primary, which was reported by the local government and to be reckoned in the income of the Budget and Expenditure (budget). The purpose of this transfer is to reduce the fiscal gap between the government and ensure the achievement of minimum standards of public services across the country (Maimunah, 2006). For the implementation of the local government authority, the central government will be transferring the balance funds to local governments. The balance funds consist of the General Allocation Fund (DAU), Special Allocation Fund (DAK), and part of the area for the central tax proceeds. In addition, the Local Government also has its own sources of funding in the form of PAD, lending area, as well as other legitimate reception area. Policy whereby the use of all funds given to local government (Prakosa, 2004). According to Law No. 33 of 2004 and Government Regulation No. 58 of 2005 Fund Balance, there are various kinds, namely DAU (General Allocation Fund), DAK (Special Allocation Fund), and revenue-sharing. DAU is allocated to the provincial and district / city. DAU scale set at least 26% of Internal Revenue (PDN) Net set in the state budget. The proportion of DAU for the province and for the district / town set in accordance with the balance of authority between the provincial and district / city. It is also stated in the Fund which is usually transferred from the central government is DAU. General allocation fund is a type of intergovernmental transfers that are not tied to specific spending programs. General allocation fund is intended to replace a subsidy transfer autonomous regions and Instruction. The purpose of this transfer is to close the fiscal gap (fiscal gap) and the ability of fiscal equalization between regions and between regions and the center. So the general allocation of each fund will not be as large area. Regions with low local revenues will get a general allocation of funds is high, and vice versa areas that have high local revenue will get a low general fund allocation.

Along passes regional autonomy, meaning that the area required to be independent in a way to maximize local revenue. It is expected that local governments can cover all forms of regional spending local revenue results. Bengkulu level mask has an area of 19,788.7 km² and is divided into 9 (nine) districts and one (1) municipal government is an autonomous region that is large enough. In 2009 the central government through Presidential Decree No.. 74 in 2008 to transfer the General Allocation Fund (DAU) to Bengkulu province of Rp487, 339,494,000 and to the district / city with details; Bengkulu city of Rp340, 287,159,000, North Bengkulu district of Rp306, 069,861,000, South Bengkulu district of Rp272, 434,666,000, Kaur district of Rp204, 909,166,000, Mukomuko district of Rp234, 105,397,000, and Rejang Lebong district of Rp321, 216,933,000. Granting transfer General Allocation Fund (DAU) is intended to finance the fiscal needs in carrying out the functions of basic public services. So that each local government spending is expected to be able to increase local revenue. Shopping area in the 2009 budget realization report obtained from the Central Statistics Agency (BPS) Bengkulu Province is described in detail; 2009 shopping areas in Bengkulu city government amounting to Rp500, 997,884,400, North Bengkulu district of Rp 452,065,000,000, South Bengkulu district of Rp393, 937 million, amounting to Rp 319,537,000,000 Kaur district, county Mukomuko of Rp440, 151 million, and the



district Rejang Lebong of Rp 519,285,000,000. While the magnitude of Expenditure (BD) of each of the local government, the amount of regional real income (PAD) in 2009 were obtained from the BPS province of Bengkulu, Bengkulu to the government amounted to Rp 28,046,719,319, North Bengkulu district of Rp19, 924 million, the district South Bengkulu Rp17, 391 million, amounting to Rp 7,641,000,000 Kaur district, county Mukomuko of Rp12, 000,000,000, and Rejang Lebong district of Rp17, 992 million. Supposed to transfer funds from the central government used effectively and efficiently by the local government to improve its service to the community. Policy use of these funds is supposed to be done in a transparent and accountable Syukriy and Halim (2003), but in practice, transfers from the central government is the main source of local government funding to finance its main operations daily. The purpose of this transfer is to reduce the fiscal gap between the government and ensure the achievement of minimum standards of public services across the country (simanjuntak in Sidik et al, 2002) and Halim Abdullah. (2003). The dependence of local governments will balance funds transferred from the central government may lead to flypaper. Bawono (2008) imply that the flypaper is a condition in which a stimulus for regional expenses caused by the change in the number of transfers from the central government greater than the stimulus caused by changes in regional income.

Previous studies that analyze the influence of the General Allocation Fund (DAU) and regional real income (PAD) against Expenditure (BD) obtain results which, regional real income (PAD) does not significantly affect the regional expenditure. That means there flypaper, which states that these results influence the allocation of public funds to the shopping area larger than the effect of local revenues to local shopping. These results are consistent with previous findings, such as Abdullah & Halim (2004), Prakosa (2004), (Maimunah, 2006), Maulida (2007) and Bawono (2008). This study is a replication of a study conducted by Bawono (2008) research which proves that the regional real income (PAD) in the current year is positive and significant effect on Expenditure (BD) of the current year. From these studies indicate that the General Allocation Fund (DAU) in the current year is positive and significant effect on Expenditure (BD) of the current year. In the current year BD prediction models, the predictive power DAU current year is higher than the revenue of the current year. Likewise with DAU last year has a greater influence than the effect of last year's revenue for the year to BD difference of this study with previous studies that used data General Allocation Fund, Local Revenue and Expenditure in the period used is the year 2004 - 2009 in district / city in the province of Bengkulu. This study took a sample of the 6 district / city in the province of Bengkulu because in 6 district / city government that there are 4 mains and 2 local government division to have complete data, whereas the flypaper to see, in this study the author uses the magnitude t values obtained from the simple regression effect of general grants and local revenues to the shopping area. Where flypaper happens if the value of t General Allocation Fund (DAU) is greater than the value of t regional real income (PAD). On the basis of the foregoing considerations, that the transfer of the General Allocation Fund (DAU) for a source of funding local government in implementing its authority. But in reality, the General Allocation Fund (DAU) is given by the central government is the main source of funding for local governments to finance local expenditure is an object that can be studied intensively, so the authors are interested in and raised in the study entitled "The Effect of General Allocation Fund (DAU) and regional real income (PAD) against Expenditure (Empirical Study on the District / City in the province of Bengkulu) ".

From some of the results of previous studies, where Effect General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD) can cause flypaper, the formulation of the problem in this study are as follows:

- 1) Is the General Allocation Fund (DAU) and of Regional Real Income (PAD) positive effect on Expenditure (BD) in the District / City in the province of Bengkulu?



- 2) What happens to the flypaper effect of the General Allocation Fund (DAU) and of Regional Real Income (PAD) against Expenditure (BD) in the District / City in the province of Bengkulu?

LITERATURE

Regional Income

Regional Income is recognized the right of local governments to supplement your net worth in the period in question (Darise, 2009). The sources of the revenue area as set out in the framework of the implementation of decentralization as stipulated in Act 32 of 2004 on Regional Government, Article 157 and paragraph 174 (4) and Article 5 of Law 33 of 2004 on Fiscal Balance between Central Government and local Government, which is defined as the sources of receipts / income areas in the implementation of decentralization consists of:

1. Regional Real Income (PAD), namely:
 - a. Results of Local Taxes
 - b. Results Retribution
 - c. Results are separated Wealth Management Regional
 - d. Other legitimate PAD

2. Fund Balance, namely:
 - a. General Allocation Fund (DAU)
 - b. Special Allocation Fund (DAK)
 - c. Revenue Sharing (DBH)

3. Others legitimate Regional Income

Regional Real Income (PAD)

Regional real income is revenue that is cultivated and managed by local authorities as well as sourced from the region itself (Mardiasmo, 2002) in Bawono (2008). According to Law No. 33 of 2004 on Financial Balance between Central and Local Government, Revenue is earned income areas based on local regulations levied in accordance with legislation. Local revenue sources of local government financing is a very important role for each of these areas, as it also depends on the ability of the region to manage and explore the potentials. In accordance with Law No. 33 of 2004 Regional Real Income (PAD) consists of:

- 1) Local Tax
- 2) Retribution
- 3) Results of the wealth management area is separated, and
- 4) Other revenue legitimate.

Other legitimate PAD referred to include:

- a) Proceeds from sales of regional assets that are not separated
- b) Current accounts
- c) Interest income
- d) Gain on the exchange rate against foreign currencies, and
- e) The commission, piece, or other form as a result of the sale and / or supply of goods and / or services by Regions.



General Allocation Fund (DAU)

General Allocation Fund (DAU) is sourced from the state budget funds allocated to bring equality between area for financial ability to fund the needs of the region in the implementation of decentralization (Law No. 33 of 2004). DAU by the central government to finance the shortfall of local governments in using PAD. General allocation fund is a type of intergovernmental transfers that are not tied to specific spending programs. General allocation fund is intended to replace a subsidy transfer autonomous regions and Instruction. General grants in Presidential Decree No. 53 Year 2009 is purely general grants as mandated by Law Number 47 of 2009 on the State Budget for Fiscal Year 2010. General allocation fund consists of:

- 1) General Allocation Fund for Provincial
- 2) General Allocation Fund for District / town

DAU is allocated to the provincial and district / city. DAU scale set at least 26% of Internal Revenue (PDN) Net set in the state budget. The proportion of DAU for the province and for the district / town set in accordance with the balance of authority between the provincial and district / city. Variable component needs fiscal (fiscal needs) are used for the calculation of DAU approach to the needs of the area consists of: population, land area, human development index (HDI), the construction cost index (CCI), and the Gross Domestic Product (GDP) per capita . While the variable component of fiscal capacity (fiscal capacity) which is a source of funding that comes from Regional Real Income (PAD) and DBH (PP. 53 of 2009). General Allocation Fund (DAU) aims for regional equalization of fiscal capacity that is intended to reduce the financial imbalance between the regions through the application of a formula that takes into account the needs and potential of the region. DAU is determined on an area the size of the fiscal gap (fiscal gap) of a region, which is the difference between the needs of the region (fiscal need) and potential areas (fiscal capacity). DAU allocation for fiscal potential large area but small fiscal needs will receive relatively small allocations, otherwise small area fiscal potential, but needs a large fiscal will obtain relatively large allocations. Fiscal gap is calculated based on local fiscal needs less fiscal capacity of the area, while the allocation is computed based on the number of local civil servants. The proportion of general fund allocation between the provincial and district / city determined by the balance of authority between the provincial and district / city. Channeling funds are held each month allocation respectively 1/12 of the general allocation fund the relevant region.

Regional Expenditure

According to Law no. 32 of 2004 on local government chapter 1 verse 16, expenditure areas are all areas obligations recognized as a reduction of net worth in the period of the fiscal year in question. Budget and Expenditure (budget) consists of budget revenues, budget, and budget financing. Budgets are prepared in accordance with the requirements of governance and regional financial capacity. No. According Permendagri. 13 In 2006 the budget is an integral structure consisting of:

- 1) local revenues
- 2) shopping area
- 3) financing area.

In Permendagri No. 59 of 2007 Article 32 par (1) in the classification of expenditure into the shopping area of government affairs consisting of obligatory spending and business spending choices. Shopping



obligatory implementation of prioritized to protect and improve the quality of life of people in order to fulfill the obligations of the area through improving basic services, education, health, social facilities and public facilities as well as developing a viable social security system, while shopping in the affairs of the options include; agriculture, forestry, energy and mineral resources, tourism, marine and fisheries, trade, industry, and transmigration. In practice, the shopping area is divided into 2 forms as contained in the Report and Revenue Expenditure Budget Actual regions, namely Routine and Development Expenditure (Bawono, 2008). According Darise (2009) shopping area qualifies under: Functions, Organizations, Programs, Activities, Group expenditure, and expenditure type. So as to facilitate the assessment of the reasonableness of the cost of a program or activity, expenditure on education in each group classified by type of expenditure and expenditure which consists of:

- a. Direct expenditure
- b. Indirect expenditure

The grouping of the reasonableness of a judgment other than the cost of a program and activities, as well as to assess the performance of each on education outcomes in accordance with the duties and functions.

1) Direct Expenditure

According Darise (2009) Direct expenditures divided by type of expenditure consists of:

a) Personnel expenditure

Personnel expenditures are used to spending honorarium / salary implement programs or activities of local government.

b) Expenditures goods and services

Spending on goods and services used for the procurement of goods and services budgeted the value of benefits less dai 12 (twelve) months in carrying out programs or activities of local governments in the form of expenditure of consumables, ingredients / materials, office services, insurance premiums, bicycle maintenance vehicles, printing / multiplication , rent house / building / warehouse / parking, mobility vehicle rental, heavy equipment rental, lease office supplies and equipment, food and beverages, clothing and service attributes, work clothing, special clothing and certain days, business travel, business travel move duties and discharge employees, maintenance, consulting services, and other goods and services, and other similar expenditures.

c) The capital expenditure.

Capital expenditures used for expenses incurred in the process of procurement of tangible fixed assets that have a value benefits more than twelve (12) months for use in government activities.

2) Indirect Expenditures

Indirect spending is spending that budgeted not affected directly by the presence of the proposed program or activity. Indirect spending is budgeted expenditures each month in the fiscal year as a consequence of local government liabilities periodically to permanent employees (salaries and allowances) and / or liabilities for other expenditures that are generally required periodically (Darise, 2009) . Where indirect expenditures have the characteristics, among others; a) budgeted each month in a year (not for any program or activity) by each on education, b) the amount of indirect expenditures are difficult to measure or difficult to compare directly with the output of a particular program or activity.

According Darise (2009) indirect expenditures divided by type of expenditure consists of:

1. Expenditures will
2. Expenditure interest
3. Spending subsidies
4. Expenditure grant



5. Expenditure social assistance
6. Expenditure for results
7. Financial Aid
8. Spending unexpectedly

Previous Research

Research on the influence of the General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD) by Bawono (2008) This study proves that local revenues in the current year is positive and significant effect on the current year's shopping areas. From these studies indicate that the General Allocation Fund (DAU) in the current year is positive and significant effect on Expenditure (BD) of the current year. In the current year BD prediction models, the predictive power DAU current year is higher than the revenue of the current year. Likewise with DAU last year has a greater influence than the effect of last year's revenue for the year to BD. Maimunah (2006) in his research found that the value of the DAU and PAD affects the value of the shopping area (positive effect). In testing this hypothesis is proven that there has been a flypaper on Expenditure on District / City in Sumatra and have occurred flypaper Expenditure in predicting future period. But on testing related to the field of Education Expenditure not happen flypaper.

Prakosa (2004) research shows that the DAU and PAD significant effect on the local shopping. While the magnitude of the number of shopping areas affected general grants received from the central government. In the shopping area prediction model, the predictive power of general grants to local expenditure remains higher than the predictive power of local revenue. This show has been going on flypaper. A similar study conducted by Abdullah and Halim (2003) study showed that separately, general grants and local revenue significantly influence the shopping area, either with or without lag. When not in use the lag, the influence of local revenues to local shopping is stronger than the general allocation fund. But by using the lag, influence the allocation of public funds to the shopping area is stronger than local revenues. This means there is a flypaper in the local government response to the general allocation fund and revenue native. When both factors (general grants and revenue) diregres simultaneously with shopping areas, they also significantly influence either with or without lag. In a prediction model without the lag, the predictive power of the general allocation fund is lower than in local revenues, but instead the power of prediction with the prediction lag the general allocation fund is higher than the revenue. Thus occurred flypaper.

Effect of General Allocation Fund (DAU) to Expenditure (BD)

Research conducted Holtz-Eakin (1985) in Maimunah (2006) states that there is a very close attachment between the transfers from the central government to the shopping area. Research Gamkhar & Oates (1996) in Prakosa, (2004) provide an analysis of the number of transfers from the federal government in the United States for the year 1953 -1991. They stated that the reduction in the number of transfer (cults in federal grants) led to a decrease in local spending. Bawono study (2008) showed that the General Allocation Fund (DAU) in the current year is positive and significant effect on Expenditure (BD) of the current year. Based on the above, the concept of hypothesis to be able to see the effect of the General Allocation Fund (DAU) to the shopping area of the current year (BD) can be expressed as follows:

H1: General Allocation Fund (DAU) positive effect on Expenditure (BD)

The influence of Regional Real Income (PAD) against Expenditure (BD)



One of the main objectives of fiscal decentralization is the creation of local independence. Local governments are expected to multiply local financial sources, particularly through revenue (Sidik, 2002) in Harianto and Adi (2007). PAD is one source of local spending, if revenue increases, the funds are owned by local governments will be higher and the level of independence of the region will increase as well, so that the local government will initiative to further explore the potential of the region and enhance economic growth. Local revenue growth in a sustainable manner will lead to an increase in the area of economic growth (Tambunan, 2006) in Harianto and Adi (2007). Local government spending will be adjusted to changes in local government revenue or income changes occur before changes in spending (Prakosa, 2004). In the international context of several studies that have been conducted to see the effect of local revenue to shopping areas such Cheng, (1999); Friedman, (1978); Hoover and Sheffrin, (1992) in Prakosa, (2004). Results from these studies is that the tax-expenditure applicable to the case of local governments in several Latin American countries, namely Colombia, the Dominican Republic, Honduras and Paraguay. Friedman in Prakosa, (2004) stated that the tax increase would increase spending hikes. Bawono (2008) The observations prove that the Regional Real Income (PAD) in the current year is positive and significant effect on Expenditure (BD) of the current year. The hypothesis that arranged to see the effect of PAD on the BD are:

H2: Regional Real Income (PAD) positive effect on Expenditure (BD)

Flypaper Effect

Flypaper is a condition in which a stimulus for regional expenses caused by the change in the number of transfers from the central government greater than the stimulus caused by changes in regional income (Bawono, 2008). Research Andersson (2002) in Prakosa (2004) on changes in the grant system of local government expenses in Sweden found that the increase in non-matching grant will cause a rise in government spending, in contrast to the result of the increase in revenue derived from taxes. High tax rate increase causes a decrease in local spending. According to Andersson, the effect of the non-matching grant greater than the matching grant and this effect depends on the relative decline over the non-matching grant for some period. These results demonstrate the occurrence of flypaper. Aaberge & Langorgen (1997) in Prakosa (2004), analyzing the fiscal and spending behavior of local government with simultaneous setting and found an area flypaper in response to changes in income.

Bawono research (2008) shows there has been a flypaper. Where expenditure policy area dominated by the number of DAU than revenue or expenditure response to the DAU different areas with reception PAD. It also shows the high dependency of local governments will block grants transferred from the central government.

So from the above description can be drawn hypotheses to see flypaper, namely:

H3: The effect of DAU against BD is greater than the effect of PAD on BD.

RESEARCH METHOD

This type of research used in this study is an empirical research. According Indriantoro and Supomo (2002), an empirical research study of empirical facts obtained by observation or experience. The object under study is more focused on the actual events than people's perception of events. Therefore, this study prioritizes research on empirical data and facts by using secondary data sources. The secondary data source of research data obtained by researchers indirectly through an intermediary medium (obtained and recorded by others).



Operational Definition and Measurement of Variables

In this study, researchers use two independent variables and one dependent variable. The variables observed in this study is the General Allocation Fund (DAU) and Regional Real Income (PAD) as independent variables and Expenditure (BD) as the dependent variable, which can be explained as follows:

1) General Allocation Fund (DAU)

General Allocation Fund (DAU) is sourced from the state budget funds allocated to bring equality among the regions financial ability to fund the needs of the region in the implementation of decentralization (Law No. 33 of 2004). General Allocation Fund (DAU) for an area is allocated by formula sebaga following:

$$DAU = \text{Fiscal Gap} + \text{Basic Allocation}$$

where,

$$\text{Cracks Fikal} = \text{Needs Fiscal} - \text{Fiscal Capacity}$$

2) Regional Income

According to Law No. 33 of 2004 revenue is earned income that is levied by the Regional District Regulation in accordance with the legislation. Local Revenue sources consist of:

- a) Local Tax
- b) Levies
- c) Results of the wealth management area is separated, and
- d) Other eligible PAD.

3) Regional Income

According to Law no. 32 of 2004 on local government, regional income areas are all obligations that are recognized as a reduction of net worth in the period of the fiscal year in question. Darise (2009) regional income consists of:

a) Direct expenditure

Direct expenditure is expenditure that is directly affected by the budgeting program or activity.

b) Indirect expenditures

Indirect spending is spending that budgeted not affected directly by the presence of the proposed program or activity. Indirect spending is budgeted expenditures each month in the fiscal year as a consequence of local government liabilities periodically to permanent employees (salaries and allowances) and / or liabilities for other expenditures that are generally required periodically.

Sample and Data Research

The research data used in this study is secondary data. According Indriantoro and Supomo (2002), secondary data is a source of research data obtained by researchers indirectly through the media perntara (dioeroleh and recorded by others). Data were taken from the financial data of the area published by the Central Statistics Agency (BPS) and the provinces of Bengkulu Regional Directorate General of Fiscal Balance (<http://www.djpk.depkeu.go.id//> site). The data used are annual data pertaining to the General Allocation Fund (DAU), the original income (PAD), and Expenditure (BD) in Bengkulu provincial



government as the period of 2007-2012. The research sample taken six (6) local government in the province of Bengkulu, which consists of 5 districts and 1 municipality. These six (6) The local government is the government district of North Bengkulu, South Bengkulu, Kaur, Mukomuko, Rejang Lebong, and Bengkulu city government. Where the local governments of the six research data can be obtained in full in the period of 2007-2012. So that data taken from six (6) district / city governments in the period 2007-2012 was obtained by 36 Data General Allocation Fund (DAU), 36 the data source revenue (PAD), and 36 Expenditure Data (BD).

For data collection techniques in this study by means of documentation, namely data collection of documents relating to the General Allocation Fund, Regional Income, and Expenditure.

Methods of Data Analysis

Classical Test Assumptions

Based on analysis tools used in this study, namely multiple linear regression analysis, the data obtained were analyzed before first performed:

1) Normality Test

This test aims to determine whether the relevant variables in the regression model and the two independent variables have a normal distribution or not.

2) Test the autocorrelation

Autocorrelation test was conducted to test whether there is a correlation between the regression model error in period t with an error in the previous period.

3) Test Multicollinearity

Multicollinearity test intended to prove whether there is a linear relationship between the independent variables (multicollinearity). Multicollinearity can be seen on the tolerance value or Variance Inflation Factor (VIF).

4) Test Heterocedastisity

Heterokedastisitas test is performed to determine whether the regression model of the residual variance occurs inequality one observation to other observations (Ghozali, 2006). Regression model is good or not happen heterocedastisity homoskedastitas.

Data Analysis Tools

The analytical tool used in this research is to use multiple linear regression equation forms and simple linear regression. In conducting the process data, researchers will be using SPSS version 16. Multiple regression equation can be written as follows:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + e \dots\dots\dots(1)$$

$$Y = \beta_1 X_1 + e \dots\dots\dots(2)$$

$$Y = \beta_2 X_2 + e \dots\dots\dots(3)$$

where:

Y: Number of Local Shopping

X1: Number of DAU

X2: Number of PAD

Bo: Konstansta

β_1, β_2 : coefficient of regression

e: Error term



Hypothesis Testing

Testing this hypothesis using a multiple linear regression analysis. Where the General Allocation Fund (DAU) and Regional Real Income (PAD) is an independent variable that affects the dependent variable prediction Expenditure (BD). To determine the influence of flypaper on the General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD) researchers used a simple linear regression analysis. By way of looking at the value of t test results separately the effect General Allocation Fund (DAU) and revenue (PAD) against Expenditure (BD). Where flypaper occur if the value of the t test results influence the General Allocation Fund (DAU) to Expenditure (BD) is higher than the value of t on the test results of the influence of Regional Real Income (PAD) against Expenditure (BD). T value is used to determine whether partially independent variable has a significant influence on the dependent variable. If the results of testing the hypothesis gained a significant level of more than 5% or 0.05 (ρ Value > 0.05) then the hypothesis is rejected. Conversely, if the value obtained is equal to or less than 0.05 (ρ Value < 0.05) the research hypothesis is accepted. Flypaper occur if the value of t General Allocation Fund is greater than the value of the original income t.

RESULTS AND DISCUSSION

Observations were made the object in this study comprises of six (6) district / city in the province of Bengkulu. Sampled local governments that have complete data is Bengkulu city government, the government of North Bengkulu, South Bengkulu, Kaur, Mukomuko, and Rejang Lebong. The data is taken from Data General Allocation Fund (DAU) and revenue (PAD) and Expenditure Data (BD) in 6 samples district / city in the province of Bengkulu during the period of 2004-2009. Data General Allocation Fund (DAU), the original income (PAD), and Expenditure (BD) is used in the form of annual data obtained from the Central Statistics Agency (BPS) Bengkulu province and the Directorate General of Fiscal Balance (site <http://www.djpk.depkeu.go.id/>).

Descriptive statistics provide a picture or description of the data that can be seen from the average value (mean), standard deviation, minimum and maximum values of each of the independent and dependent variables. Here are the results if the descriptive statistics.

Table 4.1

Total observation 6 states N = 36				
	Minimum	Maximum	Mean	Std. Deviation
BD	60.737.200.00 0,00	551.510.35 9.440,00	300.810.833.938,6 1	136.773.600.037,61
DA U	49.962.000.00 0,00	378.637.99 8.000,00	214.063.757.399,8 0	91.648.948.221,46
PAD	601.300.000,0 0	28.046.719 .319,00	10.743.160.120,05	7.117.830.077,72
Total change DAU dan PAD for 6 States N = 30				



Δ BD	123.681.84 6.568,00	180.083.4 24.826,00	58.329.172.571,43	67.349.426.354,47
Δ DAU	80.004.000 .000,00	190.149.4 70.000,00	32.217.771.886,90	56.223.169.915,90
Δ PAD	2.485.133. 381,00	9.590.287 .963,00	2.527.457.839,73	2.382.086.238,45

From Table 4.1 above it can be seen that the Expenditure (BD) for a maximum of 6 local authorities in the province of Bengkulu is Rp 551.510.359.440, 00 and Expenditure (BD) is a minimum of Rp 60.737.200.000, 00. Average Expenditure (BD) is equal Rp 300.810.833.938.61 and a standard deviation of Rp 136.773.600.037, 61. By comparing the average value Expenditure (BD) with a standard deviation of values in which the average value Expenditure (BD) is greater than the standard deviation, this illustrates that the Expenditure (BD) for 6 local government in the province of Bengkulu not too varied. Analysis of descriptive statistics for the variables next General Allocation Fund (DAU). From Table 4.1 above shows the maximum value of Rp 378.637.998.000, 00 and the minimum value of Rp 49.962.000.000, 00 as well as the average value of Rp 214.063.757.339, 80. By comparing the value of the standard deviation of the variable General Allocation Fund (DAU) of Rp 91.648.948.211, 46 whose value is smaller than the average value of the variable General Allocation Fund (DAU), concluded that the General Allocation Fund (DAU) to 6 local government in Bengkulu province are not too varied.

From Table 4.1, the variable revenue (PAD) Descriptive analysis for variable revenue (PAD) in 6 local government in the province of Bengkulu obtained that the maximum value of the local revenue amounted Rp 28.046.719.319, 00 and the minimum value of Rp 601 .300.000,00. Average revenue (PAD) is equal Rp10.743.160.120, 05 while the standard deviation is equal Rp 7.117.830.077, 72. By comparing the value of the average Regional Real Income (PAD) with a standard deviation obtained that the average value of Regional Real Income (PAD) is greater than the standard deviation, it can be concluded that the Regional Real Income (PAD) for 6 local government in the province of Bengkulu not too varied.

To see the changes Expenditure (Δ BD) in Table 4.1 Maximum values obtained Expenditure changes (Δ BD) for 6 local government in the province of Bengkulu is Rp 180.083.424.826, 00 and the minimum value of Rp-123.681.846.568.00. The average value changes Expenditure (Δ BD) amounted Rp 58.329.172.571, 43 and a standard deviation of Rp 67.349.426.354, 47. By comparing the average value Expenditure (BD) with a standard deviation values, illustrates that the Expenditure (BD) for 6 local government in the province of Bengkulu vary, it is seen from the average value Expenditure (BD), which is smaller than the standard deviation.

Furthermore, to change the General Allocation Fund (Δ DAU). In Table 4.1 for descriptive analysis of the 6 local authorities in the province of Bengkulu obtained that the maximum value for the change in the General Allocation Fund (Δ DAU) amounted Rp 190.149.470.000, 00 and the minimum value for the change in the General Allocation Fund (Δ DAU) is Rp-80 004 .000.000,00. The average change in the General Allocation Fund (Δ DAU) amounted Rp 32.217.771.886, 90 while the standard deviation amounted Rp 56.223.169.915, 90. By comparing the average values with standard deviation where the value of the average change in the General Allocation Fund (Δ DAU) is smaller than the standard deviation value. This illustrates that changes in the General Allocation Fund (Δ DAU) in 6 local government in the province of Bengkulu vary.



In Table 4.1, to see the change in revenue (Δ PAD) found that the maximum value of changes in revenue (Δ PAD) amounted Rp 9.590.287.963, while 00 is the minimum value of Rp-2485133381, 00. The average value of change in revenue (Δ PAD) amounted Rp 2.527.457.839, 73 and the standard deviation is equal Rp 2.382.086.238, 45. From the comparison of the average change in revenue (Δ PAD) with a standard deviation obtained that the average change in revenue (Δ PAD) larger than the standard deviation, then this illustrates that the change in revenue (Δ PAD) is not too varied.

Henceforth, the descriptive statistics of research variables (General Allocation Fund, Local Revenue and Expenditure) for each local government in the province of Bengkulu described in Table 4.2 below:

Table 4.2

	Minimum	Maximum	Mean	Std. Deviation
Kota Bengkulu				
BD	213.144.829.257,00	500.997.884.400,00	347.922.093.824,16	119.465.664.971,27
DAU	157.916.025.393,00	340.287.159.000,00	264.428.046.232,16	82.187.332.193,30
PAD	13.920.334.968,00	28.046.719.319,00	19.418.763.067,66	5.604.495.211,28
Kabupaten Bengkulu Utara				
BD	215.705.437.000,00	551.510.359.440,00	373.278.679.857,83	136.676.276.870,83
DAU	116.256.000.000,00	378.637.998.000,00	267.796.554.833,33	105.523.502.180,61
PAD	4.865.299.000,00	19.924.000.000,00	11.560.260.577,33	6.243.909.608,60
Kabupaten Bengkulu Selatan				
BD	115.563.215.000,00	393.937.000.000,00	268.242.512.387,50	122.704.497.229,50
DAU	87.323.000.000,00	272.434.666.000,00	197.181.212.666,66	85.032.827.260,16
PAD	4.106.789.000,00	17.391.000.000,00	10.226.341.904,83	5.041.030.153,23
Kabupaten Kaur				
BD	60.737.200.000,00	319.537.000.000,00	198.967.259.660,83	103.006.782.370,09
DAU	49.962.000.000,00	204.909.166.000,00	142.210.713.166,66	67.819.917.910,71
PAD	601.300.000,00	7.641.000.000,00	3.915.802.789,00	2.860.461.529,27
Kabupaten Muko-muko				
BD	75.807.530.000,00	440.151.000.000,00	260.833.155.962,33	152.137.977.479,55



DAU	60.311.000.00 0,00	234.105.397.000 ,00	163.734.746.500 ,00	73.558.331.636, 84
PAD	1.071.753.000, 00	12.000.000.000, 00	4.900.177.487,3 3	4.302.603.084,5 2
Kabupaten Rejang Lebong				
BD	205.362.409.0 00,00	523.398.904.205 ,00	355.621.301.939 ,00	144.832.295.649 ,57
DAU	118.963.000.0 00,00	321.216.933.000 ,00	249.031.271.000 ,00	78.185.162.721, 93
PAD	7.748.221.000, 00	20.477.133.381, 00	14.437.614.894, 16	5.236.165.934,0 8

By comparing Table 4.1 with Table 4.2 Expenditure known that (BD) on the 6 districts / cities namely Expenditure (BD) North Bengkulu district that reaches Rp 551.510.359.440, 00, whereas Expenditure (BD) were lowest in the district amounting Rp 60.737.200.000 Kaur, 319.537.000.000,00. From the comparison of Expenditure (BD) is highest with the lowest illustrates that Expenditure (BD) in 6 district / city in the province of Bengkulu vary. For variable General Allocation Fund (DAU), by comparing Table 4.1 with Table 4.2 it is known that the General Allocation Fund (DAU) obtained the highest in North Bengkulu district is equal Rp 378.637.998.000, 00 and for the general allocation Danan (DAU) is obtained at its lowest district is equal Rp 49.962.000.000 Kaur, 204.909.166.000,00. By comparing the amount of the General Allocation Fund (DAU) with the lowest highest, this illustrates that the General Allocation Fund (DAU) obtained 6 district / city in the province of Bengkulu vary.

By comparing Table 4.1 with Table 4.2 for variable Regional Real Income (PAD). Regional Real Income (PAD) obtained highest in Bengkulu city government amounting Rp 28.046.719.319, 00, while local revenue (PAD) obtained its lowest district is equal Rp 601.300.000 Kaur, 7.641.000.000,00. By comparison the Regional Real Income (PAD) highs and lows, is a portrait of that Regional Real Income (PAD) obtained in 6 district / city in the province of Bengkulu `varies.

Hypothesis Testing

Hypothesis testing is performed by multiple linear regression analysis and simple linear regression analysis. Effect of General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD) Multiple regression analysis was used to test Hypothesis 1 (H1) and Hypothesis 2 (H2), where the testing is done to find out the effect of the General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD). For the calculation of the regression of the data obtained in this study used software tools (soft ware) is a computer program SPSS version 16. Regression results can be seen in table 4.7 below:

Table 4.7

Panel A			Panel B		
Variabel	Koefisien	t-Stat. (Sig.)	Variabel	Koefisien	t-Stat. (Sig.)
Konstanta	7679316756.8 75	0.355 0.725	Konstanta	296708801856.9 94	8.198 0.000



DAU	1.263	8.193 0.000*	Δ DAU	-0.159	- 0.385 0.703
PAD	2.121 1.069	0.293	Δ PAD	15.625	1.608 0.119
R ²	0.880		R ²	0.093	
Adj R ²	0.873		Adj R ²	0.026	
F. Sig	121.011 0.000		F. Sig	1.380 0.269	
Panel C					
Variabel	Koefisien	t-Stat. (Sig.)			
Konstanta	88339081866. 425	3.261 0.003	R ²	0.787	
DAU t-1	1.205	6.148 0.000*	Adj R ₂	0.771	
PAD t-1	0.061	0.022 0.983	F Sig.	49.908 0.000	

From table 4.7 above is intended to test the hypothesis 1 (H1) and hypothesis 2 (H2) where testing hypotheses 1 (H1) aims to determine the effect of the General Allocation Fund (DAU) to Expenditure (BD) and testing hypothesis 2 (H2) aims to determine the effect of Regional Real Income (PAD) against Expenditure (BD). Hypothesis testing is done to determine the effect of the General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD) is presented in panel A.

Regression results are presented in Panel A of Table 4.7 for variable General Allocation Fund (DAU) showed a positive regression coefficient of 1.263 with a t-value of 8.193 and statistically significant at the 1% level. As for the variable revenue (PAD) also showed a positive regression coefficient of 2.121 with a t-value of 1.069 statistic and not significant at the 1% level. Of the value of t statistics it appears that the General Allocation Fund (DAU) and the Regional Real Income (PAD) positive effect on Expenditure (BD) in 6 District / City diprovinsi Bengkulu. So also of the value of the F statistic obtained for 121.011 and Adjusted R Square of 0.873. This means that 87.3% of both variables (DAU and PAD) together can explain its effect on Expenditure (BD) in this study and the remaining 12.7% is explained by other variables outside of the two independent variables in this study. Among them are sources of income other areas such as the Special Allocation Fund (DAK), Revenue Sharing, and Other Local Revenue legitimate. This means that the variable General Allocation Fund (DAU) and Regional Real Income (PAD) jointly affect positively towards Expenditure (BD) in 6 District / City diprovinsi Bengkulu. Thus hypothesis 1 (H1) and hypothesis 2 (H2) submitted acceptable.

Subsequent regression was also done by using the change (Δ) and lag (t-1) of the General Allocation Fund (DAU) and (PAD), which aims to determine the consistency of the variable General Allocation Fund (DAU) and Regional Real Income (PAD) in explaining the influence on Expenditure (BD) are presented in panel B and panel C in Table 4.7.



The test results in panel B of Table 4.7, for variable changes the General Allocation Fund (Δ DAU) showed a negative regression coefficient of - 0.159 with t statistic value of - .385 and not significant at the 1% level. As for the variable changes in Regional Real Income (Δ PAD) showed a positive regression coefficient with a value of 15.625 t statistik of 1.608 and was not significant at 1% level. Of the value of the F statistic obtained for 1,380 and Adjusted R Square of 0.026, meaning that 2.6% of both variables (DAU and PAD) together can explain its effect on Expenditure (BD) in this study and the remaining 97.4% explained by other variables outside of the two independent variables in this study. Of the value of t statistics it appears that the general allocation fund (DAU) is not a positive influence on Expenditure (BD), but rather a variable source Regional Real Income (PAD) is a positive influence on Expenditure (BD) in 6 District / City Province of Bengkulu.

In Table 4.7 C panel regression is then performed by using the lag (t-1), for the variable General Allocation Fund last year (DAU t-1) showed a positive regression coefficient of 1.205 with a t-value of 6.148 and statistically significant at the 1% level. As for the variable source Regional Real Income last year (PADt-1), showed a positive regression coefficient of 0.061 with a t-value of 0.022 statistik and not significant at the 1% level. While the value of the F statistic obtained for 49.908 and Adjusted R Square of 0.771, 77.1% means the two variables (Daut-1 and PADt-1) together can explain its effect on Expenditure (BD) in this study and the balance of 22.9% is explained by other variables outside of the two independent variables in this study. While be viewed from the value of t statistics This means that last year the General Allocation Fund (Daut-1) and the Regional Real Income last year (PADt-1) are jointly positive influence on Expenditure (BD) in 6 District / town in the province Bengkulu.

By using a multiple regression model to test the hypothesis 1 (H1) and hypothesis 2 (H2) then by taking into account the results of a panel regression in table 4.7, the equation obtained on the influence of the General Allocation Fund (DAU) and Regional Real Income (PAD) to Expenditure Cart area (BD) the county / city in Bengkulu as follows:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + e \dots\dots\dots (1)$$

the obtained equation;

$$BD = 7679316756.875 \text{ DAU} + 2,121 + 1,263 + e \dots\dots\dots \text{PAD} (1)$$

Influence on the Flypaper Expenditure

Flypaper is a condition in which a stimulus for regional expenses caused by the change in the number of transfers from the central government greater than the stimulus caused by changes in regional income (Bawono, 2008). To determine whether there flypapaer effect on the influence of the General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD) then performed a simple regression analysis. Flypapaer effect occurs when the regression results for each regression model was found turned out to be the value of t in the regression testing of the general allocation fund is greater than the value of t in the original regression income testing area to shopping area. To facilitate regression testing of the data in this study, the researchers used software tools (soft ware) is a computer program SPSS version 16. Regression results are as follows:

Table 4.8

Variabel	Koefisien	t-Stat. (Sig.)	Variabel	Koefisien	t-Stat. (Sig.)
Panel A					
DAU	1.404	40.611	PAD	24.208	16.660



		0.000			0.000
Panel B					
Δ DAU	2.477	2.701 0.011	Δ PAD	77.732	6.248 0.000
Panel C					
DAUt-1	1.573	27.527 0.000	PADt-1	28.252	12.042 0.000

A panel regression results in Table 4.8 is intended to test the hypothesis 3 (H3) where testing hypothesis 3 (H3) aims to determine whether there is flypaper on the influence of the General Allocation Fund (DAU) and revenue (PAD) against Expenditure (BD) . In panel A of table 4.8 the results of the t test statistic is obtained that the value of t Fund allocation (DAU) at 40.611 and t value Regional Real Income (PAD) of 16,660. Judging from the results of testing the value of t this means there has been a flypaper effect, since the value of t allocation fund (DAU) is higher than the value of t Regional Real Income (PAD). This means spending policy area dominated by the amount of the allocation of public funds rather than revenue. Thus hypothesis 3 (H3) proposed acceptable.

Further statistical t test was also done by using the change (Δ) and lag (t-1) of the General Allocation Fund (DAU) and Regional Real Income (PAD), in which the purpose of the test to determine the consistency of flypaper on the General Allocation Fund (DAU) and Regional Real Income (PAD) in explaining the influence on Expenditure (BD) are presented in panel B and panel C table 4.8.

Regression results in panel B of Table 4.8 is done to look at the value t of changes in the General Allocation Fund (ΔDAU) and changes in Regional Real Income (ΔPAD), test results obtained from ΔDAU t value of 2.701 and the value of 6.248 t of ΔPAD. This means that not happen flypaper effect, since the value of t changes the General Allocation Fund (ΔDAU) is lower than the value of t changes in Regional Real Income (ΔPAD).

Further to the results of the regression in table 4.8 panel C was done to see the value of t by using the lag, the results of the t test t values obtained from the General Allocation Fund last year (Daut-1) amounted to 27.527 and the value t of the Regional Real Income last year (PADt-1) amounted to 12.042. This means that there has been a flypaper effect, since the value of t General Allocation Fund last year (Daut-1) is higher than the value of t Regional Real Income last year (PADt1).

By using a simple regression model to test the hypothesis testing 3 (H3), the regression results in Panel A of Table 4.8 the equation obtained on the influence of the General Allocation Fund (DAU) and Regional Real Income (PAD) against Expenditure (BD) the county / city in Bengkulu as follows:

$$Y = \beta_1 X_1 + e \dots\dots\dots (2)$$

$$Y = \beta_2 X_2 + e \dots\dots\dots (3)$$

the obtained equation;

$$BD = 1.404 DAU + e \dots\dots\dots (2)$$

$$BD = 24.208 PAD + e \dots\dots\dots (3)$$



DISCUSSION

Discussion the first hypothesis (H1) and the second hypothesis (H2)

Based on the analysis of the results of testing hypothesis 1 (H1) and hypothesis 2 (H2) in Table 4.7 Panel A shows that the General Allocation Fund (DAU) and revenue (PAD) positive effect on Expenditure (BD) on the 6th district / city in the province of Bengkulu. These results konsiten the results of research conducted by Bawono (2008) who found that the PAD and DAU in the current year is positive and significant effect on current BD. These results are similar to Maimunah (2006) in his research that found that the value of the DAU and PAD affects the value of the shopping area (positive effect). while research Prakosa (2004) also found that the DAU and PAD significant effect on local spending.

But when seen from the regression results in Panel B and Panel C Table 4.7, where the purpose of the regression variables to determine the consistency of the General Allocation Fund (DAU) and Regional Real Income (PAD) in explaining the influence on Expenditure (BD). In panel B of Table 4.7 is obtained bring changes in the General Allocation Fund (Δ DAU) no positive effect on Expenditure (BD). While the change in (Δ PAD) actually has a positive effect on Expenditure (BD). These results are consistent with research means Bawono (2008) who found that the PAD and DAU in the current year is positive and significant effect on current BD.

Furthermore, table 4.7 C panel regression performed using lag. From the result of regression is that last year the General Allocation Fund (Daut-1) and the Regional Real Income last year (PADt-1) positive effect on Expenditure (BD) of the current year. These results konsiten with research conducted by Abdullah and Halim (2003) that separately, the General Allocation Fund (DAU) and Regional Real Income (PAD) significantly affects the shopping area, either with or without lag. It is also consistent with the theory proposed by Holtz-Eakin (1985) in Abdullah & Halim (2003) states that there is a very close attachment between the transfers from the central government to the shopping area.

Discussion of Hypothesis three (H3)

Testing the third hypothesis (H3) in Panel A Table 4.8 shows that the value of t General Allocation Fund (DAU) at 40.611 t value of local revenue (PAD) of 16,660. The regression results indicate that there has been on the flypaper effect of the General Allocation Fund (DAU) and the Regional Real Income (PAD) in 6 district / city in the province of Bengkulu. Flypaper occurs because the value of t General Allocation Fund (DAU) is higher than the value of t Regional Real Income (PAD). This means that policies Expenditure (BD) is dominated by the number of DAU than PAD. Thus hypothesis 3 (H3) stating the effect of DAU on BD is greater than the effect of PAD to BD acceptable.

This is consistent with research conducted by Bawono (2008) who found that there had been flypaper, shopping areas where policy is dominated by the number of DAU than revenue or expenditure response



to the DAU different areas with reception PAD. It also illustrates the high dependence of local governments to the general allocation funds transferred from the central government.

While the test results in panel B and panel C Table 4.8 is done by using the change (Δ) and lag (t-1) of the General Allocation Fund (DAU) and revenue (PAD). The purpose of this test is to determine the consistency of flypaper on the General Allocation Fund (DAU) and Regional Real Income (PAD) in explaining the influence on Expenditure (BD). From the test results in table 4.8 panel B t values obtained for changes in the General Allocation Fund (Δ DAU) amounted to 2,701, while the value t of changes in Regional Real Income (Δ PAD) of 6.248. These results are not consistent with the research Bawono (2008) who found that there had been flypaper, shopping areas where policy is dominated by the number of DAU than revenue or expenditure response to the DAU different areas with reception PAD.

Later in table 4.8 panel C was examined by using lag. Results obtained t value for the General Allocation Fund last year (Daut-1) is equal to 27.527 and the value of t for PAD Regional Real Income last year (PADt-1) of 12.042. This result means there is a flypaper effect, since the value of t Daut-1 higher than the value of t PADt-1. These results are not consistent with the research and Halim Abdullah (2003) where the hypothesis test is done when the lag is not used, the influence of Regional Real Income (PAD) to the shopping area is stronger than the General Allocation Fund (DAU). But by using the lag, the influence of the General Allocation Fund (DAU) to the expenditure is stronger than the Regional Real Income (PAD).

Conditions flypaper definitely a bottleneck in the implementation of regional autonomy. Because of these conditions indicate that the region is still dependent on the central government. This means that for conditions 6 district / city in the province of Bengkulu most of Expenditure (BD) sourced from the General Allocation Fund (DAU). This is due to the low Regional Real Income (PAD) to fund Expenditure (BD) in 6 districts / municipalities in the province of Bengkulu. Flypaper may occur, especially if the county or city governments was minimal local revenue.

CLOSING

Conclusion

Based on the results of the data analysis and discussion, it can be concluded:

- 1) General Allocation Fund (DAU) is a positive and significant effect on Expenditure (BD) on the 6th district / city in the province of Bengkulu. This means that the higher the General Allocation Fund (DAU) received from the central government, the greater the Expenditure (BD) issued by each district / city in the province of Bengkulu.
- 2) Regional Real Income (PAD) affects positively and significantly to the Expenditure (BD) on the 6th district / city in the province of Bengkulu. This means that the greater the Regional Real Income (PAD) does not significantly affect the magnitude of Expenditure (BD) on the 6th district / city in the province of Bengkulu.
- 3) From the results of the data analysis, it is evident that the influence of the General Allocation Fund (DAU) is greater than the effect of Regional Real Income (PAD) against Expenditure (BD).



This means that there has been a flypaper, where Expenditure (BD) is dominated by the number of general grants than the number of local revenue. This illustrates that the financing Expenditure (BD) on the 6th district / city in the province of Bengkulu is still largely dependent on the General Allocation Fund (DAU) of the other sources of revenue generated by the local government or funds received from the government balance center in addition to the General Fund allocations (DAU).

Limitations of Research

This study has the following limitations:

1. Study used a sample of only 6 studies on local government in the province of Bengkulu, Bengkulu city government namely, North Bengkulu district, South Bengkulu, Kaur, Muko-Muko, and Rejang Lebong
2. Complete data were only data from Bengkulu city government. So I find it difficult to know in detail about the allocation of public funds, Revenue, and shopping areas in each local government.

Suggestion

For further research, the authors propose the following recommendations:

1. Further studies are expected to add the sample to 10 local governments in the province of Bengkulu that the results obtained from the analysis of the data that describes the financial condition of local governments in the province of Bengkulu.
2. In this study the authors use annual data darai Data General Allocation Fund, Local Revenue and Expenditure area. So expect further research using data quarterly in order to get a more comprehensive analysis of the results.

REFERENCES

- Abdullah dan Halim. (2003). *Pengaruh Dana Alokasi Umum (DAU) dan Pendapatan Asli Daerah (PAD) Terhadap Belanja Pemerintah Daerah: Studi Kasus Kabupaten/Kota di Jawa dan Bali*. Simposium Nasional Akuntansi VI. Surabaya.
- Bawono, Bernanda. (2008). *Pengaruh Dana Alokasi Umum (DAU) dan Pendapatan Asli Daerah (PAD) Terhadap Belanja Pemerintah Daerah(Studi pada Kabupaten/Kota di Jawa Barat dan Banten)*. Yogyakarta.
- Darise, Nurlan. (2009). *“Pengelolaan Keuangan Daerah” Pedoman untuk Eksekutif dan Legislatif, Rangkuman 7 undang-undang, 30 peraturanpemerintah dan 15 Pebmendagri edisi kedua*. Penerbit PT. Indeks.
- Ghozali, Imam. (2005). *Analisis multivariate dengan program SPSS*. Semarang: Badan Penerbit Universitas Diponegoro.



Hariato dan Adi. (2007). *Hubungan Antara Dana Alokasi Umum, Belanja Modal, Pendapatan Asli Daerah Dan Pendapatan Per Kapita*.

Simposium Nasional Akuntansi X. Unhas Makassar. Kementerian Keuangan Republik Indonesia. 2010. *Sinergi Pusat dan daerah dalam pelaksanaan Desentralisasi Fiskal*. (Online) (diakses tanggal 20 Juli 2010) tersedia di www.google.com.

Maimunah, Mutiara. (2006). *Flypaper Effect pada Dana Alokasi Umum (DAU) dan Pendapatan Asli Daerah (PAD) terhadap Belanja Daerah pada Kabupaten/Kota di Pulau Sumatera*. Simposium Nasional Akuntansi IX, Padang.

Maulida, Pratiwi. (2007). *Pengaruh Dana Alokasi Umum (DAU) dan Pendapatan Asli Daerah (PAD) terhadap Prediksi Belanja Daerah. (Studi Kasus Pada Kabupaten/Kota di Indonesia)*. Yogyakarta. Prakosa, Bambang. (2004).

Analisis Pengaruh Dana Alokasi Umum (DAU) dan Pendapatan Asli Daerah (PAD) terhadap Prediksi Belanja Daerah ; Studi Empirik di Wilayah Propinsi Jawa Tengah dan DIY. (Online) (diakses tanggal 5 Mei 2010) tersedia di www.google.com.

_____. *Peraturan Menteri Dalam Negeri Nomor 13 Tahun 2006 Tentang Pedoman Pengelolaan Keuangan Daerah*. 2006. Menteri Dalam Negeri Republik Indonesia. Jakarta

_____. *Peraturan Menteri Dalam Negeri Nomor 59 Tahun 2007 Tentang Perubahan Atas Peraturan Menteri Dalam Negeri Nomor 13 Tahun 2006*

Tentang Pedoman Pengelolaan Keuangan Daerah. 2007. Menteri Dalam Negeri Republik Indonesia. Jakarta.

_____. *Peraturan Pemerintah Republik Indonesia Nomor 58 Tahun 2005 Tentang Pengelolaan Keuangan Daerah*. 2005. Sekretaris Negara Republik Indonesia. Jakarta.

_____. *Peraturan Presiden Nomor 53 Tahun 2009 Tentang Dana Alokasi Umum Daerah Provinsi, Kabupaten, dan Kota Tahun 2010*. 2009. Sekretaris Negara Republik Indonesia. Jakarta.

_____. *Peraturan Presiden Nomor 74 Tahun 2008 Tentang dana alokasi umum daerah provinsi, kabupaten, dan kota tahun 2009*. 2008. Sekretaris Negara Republik Indonesia. Jakarta.

_____. *Undang-undang Republik Indonesia Nomor 32 Tahun 2004 Tentang Pemerintahan Daerah*. 2004. Sekretaris Negara Republik Indonesia. Jakarta.

_____. *Undang-undang Republik Indonesia Nomor 33 Tahun 2004 Tentang Perimbangan Keuangan antara Pemerintah Pusat dan Pemerintah Daerah*. 2004. Sekretaris Negara Republik Indonesia. Jakarta.



Determinants Company Conditions in Disclosure Corporate Social Responsibility: Case Study in High Profile Indonesian manufacturing companies

Ninette I. Asyifa
Faculty of Economics
State University Jakarta
Jakarta
INDONESIA
ninettenia@gmail.com

ABSTRACT

Aim of this research is to analyze what are the factors that influence the disclosure of corporate social responsibility. Disclosure of corporate social responsibility is the dependent variable in this study. The independent variables were profitability, company's size, leverage and media exposure.

The samples are the high profile manufacturing companies listed on the Indonesia Stock Exchange in the year 2012. The sample was selected using purposive sampling method. Analysis data was performed with classical assumption test and hypothesis testing multiple regression analysis.

The result of this study indicates that the variable profitability and media exposure have no effect on the disclosure of corporate social responsibility. But, the company's size has a significant positive effect on the disclosure of corporate social responsibility. While the variable leverage has a negative and significant effect on disclosure the corporate social responsibility.

Keywords : Corporate social responsibility, manufacturing company

INTRODUCTION

About 50 years ago, H.R. Bowen argues that businesses's performer have an obligation to pursue a policy and make decisions or carry out various actions in accordance with the objectives and values of society (Wartick and Cochran, 1985). This argument has already given the basic framework for the development of the social responsibility concept and therefore Solihin, (2009) said that corporate behavior and the way that businesses use when running a business should be in the guide frame set society.

Nowadays in Indonesia it self, Social Responsibility mostly known as Corporate Social Responsibility (CSR) is often considered to be the core of business ethics, which means that the company not only has economic obligations and legal. This means that the company does not only have an obligation to shareholders or shareholders but also to the other parties concerned (stakeholders) whose reach exceeds it's obligations above (economic and legal).

Unfortunately, in Indonesia, there are several examples of cases related problems that arise due to the company in carrying out its operations less attention to environmental and social conditions in the surrounding areas, especially companies whose activities relating to the management of natural resources (extractive). For example, PT. Freeport Indonesia one of the largest mining companies in Indonesia are located in Papua, which started operations in 1969, up to now can not be separated from a protracted conflict with local people, both associated with communal land, customs violations, as well as social and economic disparities that occur. Buyat pollution case, the disposal of tailings into the ocean seafloor that resulted in contamination of the sea, so that reduced fish catches and declining quality of local public health due to the operational Newmon Minahasia Raya (NMR) is not only a national but an international problem. Neither violent conflict to occur due to environmental pollution and social problems related to operations of PT Caltex Pacific Indonesia (CPI) in the Duri Riau Province,



where people sue for compensation related to the level of the central Parliament negatively impact the company's operations to economic conditions, health and the environment are increasingly deteriorated (Mulyadi: 2003).

Therefore, there is government regulations that rules about the practices and encourage the disclosure of CSR in Indonesia. One of them is Limited Liability Company Law No. 40 of 2007, section 66 and 74. Article 66 paragraph (2) section c shows that in addition to financial reports, Companies are also required to report on the implementation of social responsibility and environment. In Article 74 (paragraph 1) Limited Liability Company Act provides about the company that runs its business activities in the field and / or related to all natural resources must carry out responsibilities social and environmental (Wardani:2010).

However, there is no standard about how much the disclosure of CSR and that's makes the disclosure of CSR voluntary, unaudited, and unregulated (Eka:2011). The disclosure of corporate social activity which varies may be depending on the condition of the company. Company's condition that generate high social impact will demand the fulfillment of social responsibilities of higher anyway. In this case the condition of the company that used are profitability, leverage, company's size, and media exposure (Wardani:2010).

Various studies related to the disclosure CSR shows mixed results. Some research that has been conducted shows positive relationship between disclosure CSR companies with profitability Sembiring (2005). However, several other studies showed no significant relationship between profitability and disclosure CSR Aulia (2011) and Priantinah (2012).

Various research has ever proved positive relationship between firm size variables and disclosure of CSR among others, by Sembiring (2005) and Priantinah (2013). But not all studies support the relationship between sized companies with CSR company. There is study that did not work showed a positive relationship between the two variables such, the research done by Aulia (2010).

Leverage too many variables indicated has an influence on CSR disclosure. Results of research conducted by Sembiring (2005), Aulia (2010), and Priantinah (2013) showed that leverage negatively affect CSR disclosure.

Disclosure of the media is a variable that still rarely used to describe influence on CSR disclosure. Result research conducted by Aulia (2010) showed that disclosure media had positive effect on disclosure CSR. But, Priantinah (2013) showed that media exposure had negative effect on disclosure CSR.

LITERATURE REVIEW

CSR based on Trinidad and Tobacco Bureau of Standards (TTBS) is the commitment of business to act ethically, to operate legally, and contribute to economic development along with improving the quality of life of employees and their families, the local local community, and society more broadly. While Kotler and Lee in Ismail Solihin. 2009 : 5 states that "corporate social responsibility is a commitment to improve community well-being through discretionary business practices and contribution of corporate resources".

The Definition of stakeholders explain that stakeholders have a sense as part of local community, or group of individuals, communities (not all) who came from the region's corporate standing, territory, and other countries could also (globally) who have an influence on the course of a corporate. Stakeholders and corporate influence each other, it can be seen from the social relations that shaped both responsibility and accountability. Therefore, corporate has an accountability to stakeholders (Prianthah: 2012). According to the stakeholder definition, CSR is needed to create balance and sustainability of life and relationships are reciprocal partnerships between corporate stakeholders.

The legitimacy of the organization can be seen as something that is given to the company and something that is desired by the community or sought by the people (Ghozali and Chariri, 2007). Gray et al (1996:46) in Ahmad and Sulaiman (2004) states that the organization will still exist if people realize that the organization operates on a value system that is commensurate with the value system of society itself.

Legitimacy theory advocated the companies to ensure that the activities of the company and its performance can be accepted by society. Companies use their annual report to describe the impression of environmental responsibility, so that they are accepted by society. With the acceptance of the public is expected to



increase the value of the company, thus increasing company profits. It can encourage or assist investors in making investment decisions.

Andriof and McIntosh (2001) in Solihin Ismail; 2009:147 reveal the impact of corporate operations on three areas: economic, social, and environmental. Currently various multinational enterprise revealing much that the impact that they gave on those three areas, one of which is in the field of environmental disclosure in the form of CSR disclosure.

According to Gray et. al., (1995b) in (Sembiring; 2005) there are two significantly different approaches in doing research on corporate social responsibility disclosure. First, the disclosure of corporate social responsibility may be treated as a supplement of conventional accounting activity. This approach will generally consider the financial community as the primary users of corporate social responsibility disclosure and tend to limit the perception of social responsibility are reported.

The second alternative approach is by put the disclosure of corporate social responsibility on an examination of the role of information in the public relations and organization. This broader view has been the main source of progress in the understanding of corporate social responsibility disclosure and is a major source of criticism against the disclosure of corporate social responsibility.

In some previous studies Priantinah (2012) and Aulia (2010) stated that higher profitability of the company, the more likely the ability of companies doing social disclosure. This study will examine the effect of profitability on CSR disclosure with the following hypothesis **Profitability positive effect on CSR.**

The relationship between firm size and CSR disclosure has been shown in previous studies (Priantinah, 2012; Aulia, 2010). Bigger companies can be said to have greater activity. With greater activity is based on the theory of the legitimacy of the company will engage in activities that have more social impact. Therefore, the hypothesis about the size of the company is as follows **Firm size has a positive effect on CSR.**

According Belkaoui and Karpik (1989) decision to disclose social information will follow an expenditure for the disclosure of which lowers revenues. Thus, a company with a high level of leverage would reduce social disclosure. Previous research by Priantinah (2012), Aulia (2010), and Eddy (2005) consistently show that the negative effect of Leverage on CSR disclosure. Therefore, the hypothesis about leverage is as follows **Leverage has negative effect on CSR.**

The media have an important role in social mobilization movements, such as groups that are interested in the environment (Patten, 2002b in Reverte, 2008). So, the communication functions become the basic in CSR management and through the media will improve the company's reputation in the community. The results of the study Aulia (2010) suggests that media exposure has a positive influence while Priantinah (2012) showed a negative effect. Assume the functions of the hypotheses put forward the communication relating to the influence of media exposure are as follows **The media exposure has a positive effect on CSR.**

METHODOLOGY

This study uses population that categorized as high-profile companies listed on the Indonesia Stock Exchange in 2012. Manufacturing companies included in the company's high-profile category is the construction industry, mining, agriculture, forestry, fisheries, chemical, automotive, consumer goods, food and beverage, paper, pharmaceuticals, and plastic (Fr. Reni, 2006).

The dependent variables examined in this study is the disclosure of corporate social responsibility undertaken by companies listed on the Stock Exchange. CSR indicators are annual report covering the company disclosed the theme of environment, energy, health, and safety. (Hackstone and Milne, 1996 in Sembiring 2005). If the information does not exist then the item is given a score of 0, whereas if the items of information specified in the annual report was given a score of 1.

The independent variable is a variable type that describe or affect other variables. Independent variables in this study include:

1. Profitability

In this study, the indicator used is the Return on Assets (ROA). The ROA can be calculated using the formula:

$$\frac{\text{Net Profit After Tax}}{\text{Total Assets}}$$



Total Assets

2. Company Size

In this study, the company ukursn formulated as follows:

$$\text{SIZE} = \log (\text{total assets})$$

3. Leverage

In this study, the indicators used to measure the level of leverage is the Debt to Equity Ratio (DER). The measurement using the formula:

$$\frac{\text{Total Liabilities}}{\text{Equity}}$$

4. Media Exposure

In a previous study by Aulia (2011) and Priantinah (2012) measured the media disclosure with dummy variables, namely by giving a value of 1 for companies that disclose CSR activities at the company's website, and 0 for companies that do not use CSR activities at the company's website.

Data collection methods used in this study is purposive sampling method. The data obtained through the site owned by BEI (www.idx.co.id) and corporate websites. Descriptive analysis is intended to provide an overview or description of the data that is seen from the average value (mean), standard deviation, variance, maximum, minimum, and sum. Regression testing can be performed after the model of this study meets the requirements to qualify from the classical assumptions. Where should normally distributed, contains no multicollinearity, autocorrelation, and heteroscedasticity.

Test for normality in this test aims to test is the regression model has a normal distribution. Regression of capital good is having data distribution normal or near normal. As it is known that the t test and F assumes that the value of the residuals follow a normal distribution. If this assumption is violated, the test statistic becomes invalid for small sample size (Ghozali, 2007).

Multicollinearity test aims to test whether the regression model found a correlation between the independent variables. Good regression models should not happen correlation between the independent variables. If the independent variables are correlated, then these variables are not orthogonal. Orthogonal variables are variables whose values sesame correlation between independent variables is equal to zero. (Ghozali, 2007).

Autocorrelation test aims to test whether there is a linear regression correlation between bullies error in period t with an error in period t (before). If there is a correlation, then there is a problem called autocorrelation. Autocorrelation arises because sequential observations over time are related to each other. This problem arises because the residuals so that it appears to use the time series data but the data cross-time (crosssection) and less likely to occur autocorrelation, but it will still be conducted to further convince the autocorrelation test (Ghozali, 2007).

Heteroscedasticity test aims to test whether regression occurs in the inequality of the residual variance of the observation to other observations. If the variance of the residuals of the observations to other fixed observation, hence the name, and if different homoskedasitas called heteroscedasticity. Regression model is good or not happen heteroskedasitas homoskedasitas.

In this study, multiple regression analysis is used to determine whether there is influence profitability, firm size, leverage, and media exposure to a company's CSR disclosure index. Regression model in this study are as follows:

$$Y = a + b_1X_1 + b_2X_2 + b_3X_3 + b_4X_4 + e$$

where:

Y = index of a company's CSR disclosure

A = constant

B = coefficient of regression models

X1 = Profitability

X2 = Size of Company

X3 = Leverage



X4 = Media Exposure

E = error term models

EMPIRICAL RESULTS

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
CSR_Disclosure	70	0	1	.80	.403
Profitability	70	-5.82	54.20	8.4904	10.73568
Company's Size	70	1.79	13.30	7.5327	2.80010
Leverage	70	-2.10	249.00	28.4854	46.29745
Media_Exposure	70	.00	1.00	.9000	.30217
Valid N (listwise)	70				

TABLE 1

Based on the results of the descriptive statistics table above there are 5 variables, variables of Corporate Social Responsibility, Profitability, firm size, leverage, and disclosure media. In the CSR variable indicates that disclosure smallest ratio is 0 and the largest ratio is 1. Between CSR disclosure score of 70 companies was 0.80.

The results of the descriptive statistics table shows the variable profitability that the minimum value is -5.82 and the maximum value is 54.20 with an average of 8.4904 profitability. Variable sized companies shows a minimum value of 1.79 and a maximum value of 13.30 with an average of 7.5327. The results table shows the descriptive statistics for the leverage that the minimum value of -2.10 and a maximum value of 249.00 with an average value of 28.4854. Variable media disclosure shows a minimum value of 0 and the largest ratio is 1 with an average of 0.9.

Variabel	VIF	Conclusion
Profitability	1,224	There's no Multicollinearity
Company's Size	1.188	There's no Multicollinearity
Leverage	1.031	There's no Multicollinearity
Media Exposure	1.069	There's no Multicollinearity

TABLE 2

From the table above shows that all the VIF values of multiple regression results under 10. So it can be concluded that there is no multicollinearity.

Model Summary^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.415 ^a	.172	.121	.378	2.096

a. Predictors: (Constant), Media_Exposure, Profitability, Company's Size, Leverage

b. Dependent Variable: CSR_Disclosure

TABLE 3

Of Durbin Watson table with value 5% significance level with n 70 known dL and dU of 1,343 for 1,577. The results of calculation of 2.096 Durbin Watson. This value is in the region $1.577 < 2.096 < 2.423$ so that the data can be inferred that there is no autocorrelation in the regression model.

ANOVA^b

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.924	5	.481	3.371	.014 ^a
	Residual	9.276	65	.143		



Total	11.200	70			
-------	--------	----	--	--	--

- a. Predictors: (Constant), Media_Exposure, Profitability, Companys_Size, Leverage
b. Dependent Variable: CSR_Disclosure

TABLE 4

From the above data it can be seen that the data are not hetero because the F-count > 0.05 is 3.371 > 0.05. Thus, the above data are free of the hetero.

One-Sample Kolmogorov-Smirnov Test

		Standardized Residual
N		70
Normal Parameters ^{a,b}	Mean	.0000000
	Std. Deviation	.99272718
Most Extreme Differences	Absolute	.133
	Positive	.133
	Negative	-.122
Kolmogorov-Smirnov Z		1.113
Asymp. Sig. (2-tailed)		.168

- a. Test distribution is Normal.
b. Calculated from data.

TABLE 5

Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients		Collinearity Statistics		
		B	Std. Error	Beta	t	Sig.	Tolerance	VIF
1	(Constant)	.880	.194		4.538	.000		
	Profitability	.001	.005	.016	.126	.900	.842	1.188
	Companys_Size	.044	.016	-.308	2.687	.009	.970	1.031
	Leverage	-.002	.001	.281	-2.252	.028	.817	1.224
	Media_Exposure	-.199	.156	.149	-1.276	.207	.936	1.069

- a. Dependent Variable: CSR_Disclosure

TABLE 6

Based on the results of the Kolmogrov Smirnov test that the data are normally distributed. It can be seen from Asymp. Sig (2-tailed) is 0.168 > 0.05, which means normal.



Based on the results of the overall regression calculation, the results obtained by the regression equation as follows:

$CSR = 0.880 + 0.001 + 0.044 \text{ Profitability Company Size} - \text{Leverage } 0,002 - 0,199 \text{ Media Exposure.}$

The results showed that profitability proxied by ROA showed no significant effect on the disclosure of CSR with t count of 0.126 at a significance level of 0.900 or above 0.05 probability. This means that the size of profitability does not affect the level of CSR disclosure.

Firm size is measured as total assets in the form turns out to have a significant effect with t 2.687 at significance level of 0.009. This means that the more the number, the more assets CSR disclosure by the company.

In this study it was found that leverage is proxied by DER showed significant negative effect with t count of - 2.252 at significance level of 0.028. This means that the size of the leverage negatively affects the level of CSR disclosure.

The results showed that the media disclosures had not significant effect on the disclosure of CSR with t value -1.276 at 0.207 significance level. This means that the presence of the media used by the company does not give any influence on the CSR

CONCLUSION

Based on the results of research and discussion, it can be concluded as follows:

Profitability is proxied by ROA has no effect on CSR disclosure. Firm size as measured by total assets and a significant positive effect on CSR disclosure. Leverage is proxied by DER showed a significant and negative effect on the disclosure of CSR. Disclosure of the media had no effect on CSR disclosure. Profitability, firm size, leverage, and disclosure media jointly affect CSR disclosure.

There are several limitations to this study, these limitations include the difficulty of classifying manufacturing company categorized high profile and assessment disclosure media only through the assessment of the company's website.

Based on the research results and related matters then there is some suggestion limitations, namely CSR aspect could be a consideration for investors so the companies will be trying to do the CSR disclosure in its annual report. For the further research should use sustainability reporting to be more objective and to explore the disclosure variable sample media.

References

Ahmad, N dan M. Sulaiman. 2004. "Environmental Disclosure in Malaysian Annual Reports: A Legitimacy Theory Perspective". *International Journal of Commerce & Management*. Vol.14, No.1, pp. 44-58.

Aulia Zahra Munif. (2010). *Faktor-Faktor Yang Mempengaruhi Indeks Pengungkapan Corporate Social Responsibility Di Indonesia (Studi Empiris Pada Perusahaan Non Keuangan Yang Listing Di Bursa Efek Indonesia)*. Tesis. Universitas Diponegoro.

Belkaoui, A. and Karpik, P.G. (1989), "Determinants Of The Corporate Decision To Disclose Social Information", *Accounting, Auditing & Accountability Journal*, Vol. 2 No. 1, pp. 36-51.

Eka Nanda Putra. (2011). *Pengaruh Karakteristik Perusahaan Terhadap Pengungkapan Corporate Social Responsibility (Csr)*. Skripsi Universitas Diponegoro



Fr. Reni. Retno Anggraini.(2006). *Pengungkapan Informasi Sosial dan Faktor-Faktor yang Mempengaruhi Pengungkapan Informasi Sosial dalam Laporan Keuangan Tahunan (Studi Empiris pada Perusahaan-Perusahaan yang terdaftar Bursa Efek Jakarta)*. Makalah SNA IX

Ghozali, Imam and Anis Chariri, 2007. *Teori Akuntansi*. Badan Penerbit Universitas Diponegoro : Semarang

Hackston, D and M. J. Milne. 1996. "Some Determinants of Social and Environmental Disclosure in New Zealand Companies". *Accounting, Auditing and Accountability Journal*. Vol. 9, No. 1, p. 77-108

Imam Ghozali. (2001). "*Aplikasi Analisis Multivariate dengan Program SPSS*", Semarang :Badan Penerbit Universitas Diponegoro.

Mulyadi. 2002. *Auditing: Jilid 1 Edisi Enam*. Jakarta: Salemba Empat

Priantinah, Marzully Nur Denies. 2012. "*Analisis Faktor-faktor yang Mempengaruhi Pengungkapan Corporate Social Responsibility di Indonesia*" *Jurnal Nominal*. Volume 1 Nomor 1. Universitas Negeri Yogyakarta.

Reverte, C. 2008. "Determinants of Corporate Social Responsibility Disclosure Ratings by Spanish Listed Firms", *Journal of Business Ethics* (2009) 88:351–366 DOI 10.1007/s10551-008-9968-9.

Sembiring, Eddy Rismanda. 2005. "Karakteristik Perusahaan dan Pengungkapan Tanggung jawab Sosial: Studi Empiris pada Perusahaan yang Tercatat di Bursa Efek Jakarta". *Symposium Nasional Akuntansi VIII*, Solo, 15-16 September 2005

Solihin, Ismail. (2009). "*Corporate Social Responsibility From Charity to Sustainability*". Jakarta. Salemba Empat.

Wardani, Nurul Kusuma. (2013). "*Pengaruh Karakteristik Perusahaan Terhadap Pengungkapan Corporate Social Responsibility (CSR)*". Skripsi Universitas Diponegoro.

Wartick, L. Steven, Cochran, and L. Phillip. (1985). "*The Evolution of The Corporate Social Performance Model*". *The Academy of Management Review*. Vol. 10. No. 4. October.

Ninette I. Asyifa, S. Zulaihati, S. Susanti, K.D.A. Sebayang

Faculty of Economics

State University Jakarta

Jakarta

INDONESIA

ninettenia@gmail.com,srizulaihati@yahoo.com,sanppm@gmail.com,dianta.sebayang@gmail.com



Preliminary Analysis on Related Party Transactions in Corporate Circulars

NUR SHAIDA MOHD ADNAN
School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA
shaida_adnan@yahoo.com

AKMALIA M. ARIFF
School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA
akmalia.ariff@edu.umt.my

Abstract

This study provides preliminary analysis on Related Party Transactions (RPTs hereafter) in circulars issued by companies in Malaysia. We review existing rules and regulations on disclosure of RPTs information in Malaysian context and highlight issues regarding the importance of the information. A disclosure index is used to derive information about the types of transactions, the types of related parties (RPs) and the amount of RPTs. The analysis shows that most of the companies have disclosed their RPTs and RPs with specific information. The information disclosed can assist users of circulars to evaluate the RPTs of the companies.

Key Words: Related Party Transactions, circulars, Malaysia

1. INTRODUCTION

This study reviews Related Party Transactions (RPTs hereafter) information in corporate circulars in Malaysia. RPTs are transactions between a firm and related entities (Gordon, Henry, Louwers, & Reed, 2007). RPTs include ordinary business transactions, such as purchase or sale of goods, property or other assets, and loans and guarantees, which are done with a related party. Related parties (RPs hereafter) refer to a person or entity that is related to the reporting entity which consists of management, board members, principal owners, or members of the immediate families of any of these groups (Gordon et al., 2007).

In the context of Asian countries, including Malaysia, cases of abusive RPTs are noticed. One of the reasons is because the landscape of business in the country is more to the family or state run business groups. Further, informal nature of business relationship facilitates abusive RPTs in Asia (OECD, 2009). Example of RPTs issues reported in the media is the case of Ho Hup Construction Company Bhd (Chan, 2010). Nevertheless, there are regulations that are put in place to govern RPTs. In Malaysia, four sources of regulations involving RPTs are mainly applicable; MFRS 124, Policies and Guidelines on Issue/offer of Securities Commission of Malaysia, Bursa Malaysia Listing Requirements, and the Companies Act 1965. The aim of the regulations on RPTs is to ensure that



the RPTs are developed to be in the best interests of a company and must not be detrimental to the company's minority shareholders. To achieve that aim, among the important requirement of the regulations is for firms to disclose relevant and sufficient information regarding their RPTs. This is because appropriate disclosure of RPTs information in corporate reports would allow users to monitor and evaluate the risks and opportunities arising from the RPTs.

Realising the importance of RPTs information, the objective of our study is to perform a comprehensive analysis on the disclosure of information about RPTs in corporate circulars. Prior studies, which tend to rely on the mere existence of RPTs and/or amount of RPTs, may not be able to capture the wide range of RPTs that may have different implications on firm. Prior studies also tend to focus on the annual report that may not be as timely as circulars in providing information on RPTs. Our study, therefore, add to the literature by exploring more about the nature and types of RPTs that are commonly used by companies in Malaysia. Findings of our study may be able to assist users of corporate report in assessing the impact of RPTs on a firm's performance in their decision-making.

In our analysis, we review RPTs information disclosed in corporate circulars. A circular is an important corporate report as the document outlines important matters to be discussed at the annual meeting, or at an extraordinary meeting. We develop a disclosure index to assess the level of disclosure regarding the types of transactions, the types of related parties, and the amount of the RPTs. Our preliminary analysis on 20 circulars shows that companies disclose their RPTs and RPs comprehensively. The information disclosed can assist users in evaluating RPTs of the companies.

In this study, Section 2 discusses the literature about RPTs and issues related to disclosure of RPTs information. In Section 3, we review the rules and regulations of disclosure about RPTs in Malaysian context. Section 4 provides details about the information required on RPTs, Section 5 analyses the information of RPTs in circulars, while section 6 concludes.

2. RELATED PARTY TRANSACTIONS (RPTs) AND RELATED PARTIES (RPs)

MFRS 124 defines RPTs as a transfer of resources, services or obligation between a reporting entity and a related party, not considering of whether a price is charged. Example of RPTs are purchase or sale of goods, property or other assets, and leases (MASB, 2013). According to MFRS 124, RP is a person or entity that is related to the reporting entity i.e. entity that prepares financial statements. RPs can be close family members, board members, managements and principal owners. Parties are deemed related if one party has the ability to control the other party or to exercise significant influence or joint control over the other party in deciding on financial and operating issues (MASB, 2013). Besides, entities that control the financial statements, or controlled by another entity, which also controls the financial statement, are known as related parties.

Securities Commission of Malaysia describes RPTs as any transaction that involve the acquisition or disposal of interest, whether in securities or assets, by a public listed company or any of its to related parties. RPs can be a substantial shareholder of the company, a director of the company, or any other company which is its subsidiary or holding company or a subsidiary of its holding company or an associate of a related party (Securities Commission Malaysia).

The Bursa Malaysia Listing Requirements defines RPTs as transactions entered into by the listed issuer or its subsidiaries. RPs involve the interest, whether direct or indirect, of a director, major shareholder or person connected with the director or major shareholder. Even a past director or major shareholder is considered as related parties for transaction that is made within six months after one ceased to hold that position (Chan, 2010).

RPTs exist when the transfer of resources, services, or obligations occurred between RPs. RPTs can also be classified into recurring or non recurring transaction. Recurring Related Party Transaction (RRPTs) refer to related party transactions which are recurrent, of a revenue or trading nature and which is necessary for day-to-day operations of a listed issuer or its subsidiaries (Bursa Malaysia Listing Requirements, Part E, Section 10.02, Para



J). RRPTs can exist, for example, in transactions involving sales and purchases of goods and services. Usually, it happened when suppliers and/or customers of a reporting entity are group companies. Non-recurring RPTs are quite common in transactions involving transfer of assets. In Asian companies, the assets to be transferred are often land and/or property (OECD, 2009).

RPs can either be those who are deemed to be related, or those where a related party relationship is presumed. Deemed relatedness refers to the transactions with directors, group members, associates and joint ventures. Presumed relatedness can exist in cases involving key management and close family members. Relatedness could extend both horizontally and vertically around the ownership (OECD, 2009). For example, there can exist several threshold tiers of family relationships: a) at the first level, spouse, brother, sister, mother, father, son, daughter, or equivalent; b) at the second level, cousins, in-laws, aunts, uncles, or equivalent; and c) at the third level, grandparent, grandson, or equivalent. In Huang and Liu (2010), RPs consist of the reporting entity's management, board members, principal owners, or members of the immediate families of any of these groups. Entities that control the reporting entity, controlled by the reporting entity, or controlled by another entity that also controls the reporting entity are also considered as related parties.

2.1 The importance of RPTs issue in Malaysia

While RPTs are normal business transactions, abusive RPTs are a significant corporate problem in Asia, including in Malaysia. In Asia, family (or state-run) business groups and the informal nature of relationships that exist in doing businesses facilitate abusive RPTs. Abusive RPTs are often accompanied by a loss of business opportunity for the listed entity, led to overpayment of an asset, or placed the entity at substantial risk (OECD, 2009). Abusive RPTs put companies at risk as they can further lead to fraud or accounting irregularities. Besides, abusive RPTs may lead to 'national' discount to the country's market as a whole (OECD, 2009).

The case of Singapore listed Pacific Century Regional Development shows management misrepresenting their financial statements, including by means of related party transactions, in order to meet market expectations under strong pressure from shareholders. In any event, abusive related party transactions damage market integrity considerably. Other highlighted cases about abusive of RPTs in Asia are Satyam case in India regarding bail out, CNOOC Ltd in Hong Kong regarding cross guarantee and loans to affiliates and tunneling of assets, and Daewoon Corp in Korea, regarding assets swap, loans and subsidies (OECD, 2009).

Abusive RPTs are also noticed in Malaysia. Chan (2010) discusses the issue of RPTs involving Ho Hup Construction Company Bhd ("Ho Hup"). In that case, Low Chee & Sons Sdn Bhd, a major shareholder of Ho Hup instituted legal action against Ho Hup regarding a purchase of land. Evidence indicates that there is a conflict of interest about relationship of the related party but for reasons not revealed, Low Chee & Sons withdrew their suit. In 2012, Bursa Malaysia in its media release highlights a case that relates to a proposal announcement by BlueFire Capital Group to acquire the entire business and undertakings of KNM. RPTs exist in this situation, as BlueFire Capital Group is an entity controlled by the KNM GROUP's Managing Director. The company's directors approved the announcement, even though there is lack of disclosure on some material information related to the Conditions of the offer. In this case, the company and eight of its directors are publicly reprimanded and fined a total of RM 200,000. It is probable that the approval decisions could be made due to conflict of interest that exists, rather than the directors' true understanding on nature of the transactions (Ariff & Hashim, 2014).

In general, abusive RPTs can potentially occur because some RPTs are embedded in documentation that is less clear or thorough than the documentation that ordinarily exists in transactions with unrelated parties. RPTs can also be transactions that are very complex in nature that makes it easy for them to escape from the auditors and regulators oversight. Therefore, it is important for users of corporate report, such as circulars, to be provided with appropriate information regarding RPTs to enable them to understand the effect of RPTs.

2.2 The Dual Effect of RPTs

RPTs, which can be made through simple or complicated transactions, are complex issue. On the whole, there are



two opposing theories regarding the relationship between RPTs and firm value, which makes it unclear as to whether RPTs are value enhancing or value destroying for a firm and its' shareholders.

From the perspective of the efficient transactions hypothesis, Gordon et al. (2004) suggests that RPTs are sound business exchanges that fulfill the economic needs of the firm. Ge et al. (2010) argue that RPTs are beneficial to a company as they can reduce transaction costs, optimize internal resource allocation, and improve return on assets. There are three reasons to support the perspective of efficient transactions hypothesis. First, RPTs can lead to contracting efficiency because related parties can draw up a contract more quickly and avoid the obstacles often experienced with non-related parties. Secondly, RPTs offer strategic feedback as persons affiliated with the company may be able to provide relevant knowledge that is required to make reasoned decisions. A third benefit of RPTs is the facilitation of investment for which a company may be able to resort to a better financing option at the time of financial distress. RPTs with these motivations, if they translate to good operating results, could be value enhancing to shareholders.

While the great majority of related party transactions are in the normal course of business, there are RPTs that are detrimental to the shareholders' wealth. One classic example is shown in the case of Enron, where RPTs were used to conceal debt as well as billions of dollars in self-serving transactions. RPTs that are tainted with conflicts of interest can lead to the potential expropriation of the firm's resources (Gordon et al. 2004). From the perspective of principal-agency conflicts theory by Berle and Means in 1932, RPTs are economically harmful for the firm. For example, by depositing its surplus cash in an unlisted parent for an indefinite period, a listed company is denying its minority shareholders the opportunity to generate higher return through strategic investments. Another example is by purchasing assets from unlisted affiliates at an inflated price, a listed company is channeling the fortunes of the public entities into the private interests of the same controlling shareholders. Therefore, Kohlbeck and Mayhew (2010) argue that RPTs raise agency problems due to the possibility that managers will over consume perquisites and alter the reliability of financial statements to facilitate abusive RPTs. These abusive RPTs are value destroying to shareholders as they are channels for the expropriation of their wealth.

In summary, although RPTs are not necessarily wrong, and are legitimate activities which are recognized in corporate and taxation laws, transactions that involve related parties must be carefully scrutinized and the related information must be fully disclosed. Further, the environment that surrounds corporate activities influences whether RPTs are 'good' or 'bad'. In general, RPTs are supposed to have the prior consent of shareholders, and are subject to disclosure and ceilings in respect of contract value.

3. DISCLOSURE REQUIREMENTS AND INFORMATION REQUIRED ON RPTs

RPTs are one of the important information required to be disclosed in corporate reports. In Malaysia, the disclosure requirements for RPTs have been described in several standards and regulations. They are MFRS 124, Bursa Malaysia Listing Requirements, Securities Commissions in Malaysia, and Companies Act 1965. In general, public listed companies in Malaysia have to adhere to this standards and regulations involving RPTs.

3.1 Disclosure Requirements for RPTs

The accounting standards in Malaysia, including the standard that prescribes the accounting and reporting for RPTs, have gone through several changes throughout the period. More recently, as part of the plan to bring Malaysia to full convergence with IFRS, the Malaysian Accounting Standards Board (MASB) introduced a new IFRS-compliant framework ("MFRS Framework" hereafter) to be effective 1 January 2012. In the MFRS Framework, RPTs are covered in MFRS 124 that contains standard that are similar to the International Accounting Standards on RPTs (IAS 24). MFRS 124 prescribes the requirements regarding disclosure of RPTs in financial statements and notes to the financial statements. The objective of the Standard is to ensure that the disclosure in the financial statements are sufficient enough to detect the possibility that the financial position and profit or loss may



have been affected by the RPTs (MASB, 2013). The standard describes about RPTs and RPs in detail. MFRS 124 requires disclosure of RPTs and outstanding balances in the separate financial statements of a parent, venture or investor (Liong Tong, 2012). The requirement in MFRS 124 is in addition to the requirements for disclosure in MFRS 127, MFRS 128, MFRS 131, and MFRS 101.

Bursa Malaysia Listing Requirements emphasize that RPTs must be developed to be in the best interests of a public listed company and must not be detrimental to the company's minority shareholders. The objective of Bursa disclosure requirement is to allow monitoring on any transaction that presents a potential risk of abuse. Chapter 10 of the Bursa Malaysia Listing Requirements sets out the requirements in respect of transactions related to the RPs. The disclosures required by Bursa are 1) particulars of material contracts involving directors' interests; 2) a statement to set out the names of substantial shareholders and the number of equity securities in which they have an interest; and 3) the names of the 20 largest holders of each class of equity securities and the number of equity securities of each class held (Liong Tong, 2012).

Requirement for RPTs disclosure are also detailed in Chapter 20 of the Policies and Guidelines on Issue/offer of Securities Commission of Malaysia. Besides defining RPTs and RPs, the guidelines require firms to; a) provide announcement containing brief details of RPTs, b) submit circulars to shareholders for the purpose of providing information regarding the nature and types of transactions and related parties and their relationship, which are to be attached with recommendation letters from independent directors, board of directors, and independent advisers, c) acquire approval of its shareholders, and d) ensure that the related party abstains from voting on the relevant resolutions (Ariff & Hashim, 2013). However, firms are exempted from requirements in the case; a) where the transactions is an issue of new securities available for cash to all holders or made pursuant to the exercise of conversion or subscription rights attached to a class of securities, b) where the transactions involve the receipt of securities in the listed public company by a director of the company, its parent company or any of its subsidiaries; or a grant of an option to a director of the listed public company, its parent company or any if its subsidiaries to acquire new securities of the public company or any of its subsidiaries (Liong Tong, 2012).

The Companies Act 1965 has many provisions that focused on governing a company's transactions, including on RPTs. The provision that prohibited transactions with its directors and persons or corporations connected or related parties, with the directors, and with substantial shareholders are stated in Ninth Schedule of Companies Act 1965. Information about specific disclosures of information about related party relationships and of transactions with its related parties is required. Mainly, the Ninth Schedule requires two types information; for the profit and loss and the balance sheet. For the profit and loss disclosures, information related with gross income from investments in subsidiaries and director's remuneration should be disclosed. For the balances sheet disclosures, information that should be disclosed are the investments in subsidiaries, amounts owing by the holding company, amounts owing by subsidiaries, amounts owing by other related corporations and vice versa (Liong Tong, 2012).

INFORMATION REQUIRED ON RPTs

Transactions between related parties commonly occur in the normal course of business. MFRS 124 recognizes several types of RPTs. They are classified as: (1) purchases or sales of goods and services (finished and unfinished), (2) purchases or sales of property and other assets, (3) rendering or receiving of services, (4) leases, (5) transfer of research and development, (6) transfer under license agreements, (7) transfer under finance arrangements (including loans and equity contributions in cash or in kind) and (8) provision of guarantees or collateral. Besides MFRS 124, there are several other classifications of RPTs that can be found in prior studies.

In Amzaleg and Barak (2013), RPTs are divided into three categories that are fiscal transaction, financial transaction, and compensation transaction. Kohlbeck and Mayhew (2004) classify RPTs into ten categories. However, they see two distinct groupings after their detailed reading of the footnotes. The first group refers to specific RPTs, for which the disclosure is normally very clear as to their financial statement impacts. Examples are loans, leases, guarantees, consulting, legal, and investment services. These kinds of transactions are rather



straightforward. The second group is ambiguous RPTs, for which the financial statement impact is generally not obvious from the disclosure. Examples of ambiguous RPTs are business transactions, overhead reimbursement plans, and stock transaction.

Gordon and Henry (2005) identify seven main categories of RPTs. They are (1) direct service between RPs or the RP and the company, (2) purchases of goods or contract services acquired from the RPs, (3) sales to the RPs, (4) loans to RPs, (6) fixed-rate financing from RPs, investment, and (7) others. Contracted services acquired from the RPs can be management services, marketing, real estate, accounting, and others. They also identify transactions involving purchases of goods from the RPs and classify loans into those to the related party for houses and stock purchases, where specified, or other, where another purpose is given or none is identified. They separately identify fixed-rate financing from the RPs, which can be in the form of loans or preferred stock, sometimes with conversion features or warrants. The “other” category includes other types of transactions such as shareholder agreements and shared R&D.

Cheung et al. (2009) analyze connected transactions into three categories: a) transactions that are a priori to result in expropriation (asset acquisitions, asset sales, equity sales, and trading relationships and cash payments), b) transactions that are of likely benefit to the listed firms (cash receipts and subsidiary relationships), and c) transactions that may have been driven by a strategic rationale (takeover offers and joint venture stake acquisitions and sales). Ryngaert and Thomas (2012) classify RPTs as either being “ex ante” or “ex post” transactions. Ex ante RPTs are defined as transactions that originate before a firm becomes a publicly traded entity or before the counterparty becomes a related party. In the case of ex ante RPTs, they posit that it is unlikely that insiders use their power to enter into these transactions to the disadvantage of outside shareholders as the transactions are arm’s-length when initially negotiated. However, ex ante transactions are subject to reporting as RPTs under current disclosure requirements, and it is possible that the continuation and renegotiation of the terms of these transactions is subject to the potential conflict of interest created by the counterparty becoming a related party. Meanwhile, ex post RPTs are those that occur after the firm goes public and after the counterparty to the transaction obtains related party status. They argue that ex post RPTs are not arm’s-length in nature and may be more likely be used to expropriate value from outside shareholders.

In short, there are many types of RPTs that can be performed with many types of RPs making RPTs as a complex transactions that a firm can undertake.

4.1 The need for disclosure of information about RPTs

The importance of RPTs information is highlighted by prior studies. Gordon, Henry, and Darius (2004) state an appropriate disclosure of RPTs information in corporate reports would be able to protect the stakeholders' interest. This is because such approaches provide them with necessary information to assess the effect of these transactions, which, at the same time become an efficient measure to prevent misappropriation of the company’s resources through various means. Gordon et al. (2004) also state that if companies commit to fully disclose RPTs information, investors and other users of corporate reports would be able to monitor and evaluate the impact of the RPTs on the performance of the companies.

Further, when disclosures are made separately for each categories of related party, a more comprehensive analysis of RPTs can be made. Disclosure regarding the relationships between companies and RPs are required to enable corporate statement users to develop their views about the effects of RP relationships on firm (Munir & Mohd-Saleh, 2009). Investors can rely on the disclosures to judge whether the RPTs are value-enhancing or value-destroying. Investors can evaluate the effect of RPTs on the profit or loss and financial position since RPs may enter into transactions that unrelated parties would not. For example, an entity that sells goods to its parent at cost might not sell using the same terms to other customer. So, disclosure of RPTs may affect assessments of its operations by users of financial statements, including assessments of the risks and opportunities facing the entity (MASB, 2013).



RPTs IN CIRCULARS

5.1 Requirement for RPTs in Circulars

A circular is a document submitted to shareholders that outline important matters to be discussed at the annual meeting (AGM), or at an extraordinary meeting (EGM). The purpose of circular is to set out details of and information relating to a proposal, and board's recommendation thereon, and to seek approval for the relevant resolution relating to the proposal. The circular needs votes from shareholders and provides information on procedures to vote on key issues. Supporting documents that should be enclosed together with the circulars are letters of recommendation from independent directors, board of directors, and independent advisers. The printed circular must be issued to the Exchange immediately upon receipt of confirmation that it has no further comments thereon and in any event no later than 7 market days after receipt of such confirmation (Bursa Malaysia Listing Requirement, Part I, Section 8.30).

According to the Bursa's Listing Requirement, RPTs information that needs to be disclosed in circular to shareholders are announcement dates, nature of transactions, types of transaction, related parties and their relationships, amount transacted, and owning (from previous RPTs). These information need to be disclosed to assist shareholders in their voting decision.

5.2 Sample and Data Collection

In this study, we review circulars of public listed companies in Malaysia from 1 January 2012 until 31 December 2013. The circulars of the companies are available from the Bursa Malaysia website. We include all sectors from the main market excluding financial and REITS companies. In the website, the total of the circulars during the period is 1,901. However, there are only 739 circulars that contain information about RPTs.

Abdul Wahab et al. (2011), which look into RPTs in circulars in Malaysia, recognize two main types of RPTs. They are RPTs that needed independent advice and recurrent RPT (RRPT). In their study, they identified the number of RPTs and the amount of each transaction. As compared to Abdul Wahab et al., (2011), this study analyses more comprehensive information on RPTs using a disclosure index. In the index, we classify the RPTs information into three categories. There are the types of transactions, types of relationship, and amount of transactions. These categories are derived from the components of disclosure required by the regulations and previous studies (e.g., Kohlbeck & Mayhew, 2010).

For types of RPTs, we follow Kohlbeck and Mayhew (2010) which classify RPTs into two categories. There are simple/specific RPTs and complex/ambiguous RPTs. The specific RPTs is defined the disclosure where it is normally very clear as to a financial statement impacts. They refer to loans, leases, guarantees, consulting, legal and investment services. The ambiguous RPTs is defined as those where the financial statement impact is generally not obvious from the disclosure. Ambiguous RPTs include business transactions, overhead reimbursement plans, and stock transaction.

For types of RP relationships, we mainly adapt the classification in Gordon and Henry (2005) and Kohlbeck and Mayhew (2010). There are three categories of RP relationships. They are primary related parties, secondary related parties, and investments. The primary related parties are defined as the party having the most direct or most senior relationship with the firm. They refer to officers, directors and major shareholders. For example executives, non-executive board members, principal owners and subsidiaries. The secondary related parties are defined as the family member or company owned by or affiliated with the primary related party. They refer to affiliates of officer, directors or shareholders. For investments, related party is defined as a joint venture or other operation in which the company has a less than 100% investment that is not consolidated.

For amount of RPTs, we refer to total consideration of RPTs (in Ringgit Malaysia). The amount of each transaction is recorded to measure the value of RPTs disclosures. The dollar amount of each transaction was recorded to measure the magnitude of RPTs.

To evaluate the information on RPTs, this study develops a coding system to score discretionary information



provided in corporate circulars. This approach is taken in order to capture the variations and quality of RPT disclosure practices by companies in Malaysia. We use a 0 – 3 scoring system to measure the extent of RP disclosure. While firms have to comply with mandatory requirement of Bursa Malaysia Listing Requirement, the level of disclosure may vary in term of the quality of the information as certain information requires managerial description. Therefore, the coding system is defined by the quality of information disclosed about RPTs. Each sentence will be given a ‘qualitative’ score, based on the perceived informative of the information disclosed. Score range from ‘0’ to ‘3’ based on a scale where the greater the specification of the information, the more useful it is deemed to be and, hence, of quality. The score is 0 if the companies do not have any information disclosed in their circular. The score is 1 if the level of disclosure RPTs information is low. The score is 2 if the level of information is moderate. The score is 3 if the level information disclosure is high.

5.3 Findings on RPTs in Circulars

For the preliminary analysis, we review 20 of the 739 circulars. Table 1 provides the detailed information about disclosure of RPs and RPTs information in circulars. In Table 1, the information from the circulars are tabulated into types of RPTs, types of RPs and the total amounts of RPTs. For RPTs, we divide into three sections which are i) number of transactions, ii) the score for the quality of the disclosed information, and iii) types of RPTs. For RPs, we also divide into three sections which are i) number of RPs, ii) the score for the quality of the disclosed information, and iii) types of RPs. The last column in Table 1 displays the amount of RPTs in Ringgit Malaysia.

<Insert Table 1>

Based on Table 1, the average number of types of RP transactions is 2. The most common types of transaction are sales and purchases of inventory, while the less common type of RP transaction are sales and purchases of asset. Two companies, Batu Kawan Berhad and Berjaya Media Berhad, have the highest number of types of RPTs with 6 types of transaction each. For types of related parties, the average number of types of RPs is 2. The most common types of RPs are ‘person connected’ and the less common type is ‘associates’. Batu Kawan Berhad has the highest number of types of related parties, which is 5 types. The average amount of RPTs is RM55, 711,775. The highest amount of RPTs is RM492, 721,000, which is by PERSTIMA Bhd. Meanwhile, the least amount of RPTs is by Brahim’s Holding Berhad, which is only RM3, 000.

The results show that most of the companies have disclosed their RPTs with specific transactions such as purchase of raw material. They also disclose their RP relationship with additional information. For example, person connected with director of the company is detailed as to whether they are siblings or spouse. Overall, the information of RPTs and RP relationship has been disclosed comprehensively in corporate circulars.

6. CONCLUSION

This study reviews the existing rules and regulations of disclosure of RPTs information in the Malaysian context and analyses the RPTs information in corporate circulars. We examine the extent of RPTs using a disclosure index. Using 20 samples of circulars from companies in Malaysia, we find that most Malaysian companies disclose their RPTs comprehensively. The information disclosed will help users of circulars to understand the quality of information, especially about RPTs.

**Table 1: Information about RPTs in Circulars**

no	COMPANY & DATE	RPTs			RP			TOTAL
		no of transactions	scoring	types	no of related parties	scoring	types	
1	Chin Teck Plantations Berhad 9-Jan-12	1	3	purchase	1	2	person connected	5,000,000
2	Concrete Engineering Product Berhad 18-Jan-12	2	3	sale	1	2	subsidiary	10,000,000
				purchase				
3	Melati Ehsan Holding Berhad 3-Feb-12	2	3	the provision by the companies	4	2	director	330,000,000
				shareholder				
				major shareholder				
rental	person connected							
4	Pelangi Publishing Group Bhd 29-Feb-12	4	3	sale of asset	2	3	director	15,158,000
				renting of premises				
				purchases				
				receiving of services			person connected	
5	Brahim's Holding Berhad	1	3	provision of guarantees	1	3	person connected	3,000
	19-Apr-12							
6	Turbo-Mech Berhad 3-May-12	2	3	sale	2	2	person connected	8,150,000
				provision of guarantees			associates	
director								
7	Timberwell Berhad 23-May-12	2	2	leases	2	2	person connected	6,000,000
				advances and interest payment			director	
8	Nagamas International Berhad 1-Jun-12	1	2	purchase	2	1	director	5,000,000
							major shareholder	
9	Luster Industries Berhad 14-Jun-12	3	3	sale	3	2	person connected	4,550,000
				purchase			shareholder	
				rendering of services			director	
10	Perusahaan Sadur Timah Malaysia (PERSTIMA) Berhad 27-Jun-12	2	3	purchase	2	2	director	492,721,000
				sale			person connected	
11	JAVA Berhad	2	3	purchase	3	2	person connected	112,450,000
							subsidiary	



	25-Sep-12			provision services			major shareholder	
12	The Store Corporation Berhad 6-Mar-13	1	3	rental	1	2	subsidiary	11,213,114
13	ALLIANZ Malaysia Berhad 30-May-13	3	3	transfer under finance purchase software(asset) receiving of services	1	2	major shareholder	426,942,500
14	KNM Group Berhad 5-Jun-13	2	3	leases provision	3	2	person connected major shareholder director	35,500,000
15	Hartalega Holdings Berhad 6-Aug-13	3	2	purchase sale	1	2	subsidiary	1,440,974.56
16	Berjaya Media Berhad 13-Sep-13	6	3	sale rendering of services transfer under finance rental leases purchase asset	2	3	major shareholder subsidiary	28,156
17	London Biscuits Berhad 5-Dec-13	2	0	purchase sale	1	0	directors(key management personnel)	116,000,000
18	Poh Kong Holdings Berhad 19-Dec-13	4	2	sale purchase receiving of services rental	3	3	person connected directors major shareholder	7,850,000
19	Batu Kawan Berhad 27-Dec-13	6	3	purchase raw material provision of services rental receiving of services sale	5	3	person connected major shareholder director subsidiary associates	770,000,000
20	Fraser & Neave Holding Berhad 30-Dec-13	4	3	sale receiving of services rental purchase	2	3	subsidiary person connected	463,082,000



References

- Abdul Wahab, E. A., Haron, H., Lok, C. L., & Yahya, S. (2011). Does Corporate Governance Matter ? Evidence from Related Party Transactions in Malaysia. In K. John & A. K. Makhija (Eds.), *Advances in Financial Economics* (First edit., Vol. 14, pp. 131–164). Bingley, UK: Emerald Group Publishing Limited. doi:10.1108/S1569-3732(2011)0000014009
- Ariff, a. M., & Hashim, H. a. (2013). The Breadth and Depth of Related Party Transactions Disclosures. *International Journal of Trade, Economics and Finance*, 4(6), 388–392. doi:10.7763/IJTEF.2013.V4.323
- Ariff, a. M., & Hashim, H. a. (2014). Accounting Irregularities in Related Party Transactions. *International Journal of Trade, Economics and Finance*, 5(2), 180–183.
- Berle, A. A., & Means, G. C. (1932). *The Modern Corporation and Private Property*. New York: The Commerce Clearing House.
- Bursa Malaysia. Chapter 10, Bursa Malaysia Listing Requirement (2013). Malaysia.
- Cheung, Y., Qi, Y., Rau, P. R., & Stouraitis, A. (2009). Buy high, Sell low: How Listed Firms Price Asset Transfers in Related Party Transactions. *Journal of Banking and Finance*, (33), 914–924.
- Chan, W. M. (2010). Expropriation Through Related Party Transactions : The Position In Malaysia. In *The Applied Business Research (ABR) and College Teaching & Learning (TLC) Conferences* (pp. 1–11). Orlando.
- Ge, W., Drury, D. H., Fortin, S., Liu, F., & Tsang, D. (2010). Value Relevance of Disclosed Related Party Transactions. *Advances in Accounting*, 26(1), 134 – 141. doi:10.1016/j.adiac.2010.02.004
- Gordon, E. A., & Henry, E. (2005). *Related Party Transactions and Earnings Management* (pp. 1–37). Retrieved from <http://ssrn.com/abstract=612234>
- Gordon, E. A., Henry, E., & Darius, P. (2004). Related Party Transactions : Associations with Corporate Governance and Firm Value. In *European Finance Association Annual Conference* (pp. 1 – 59). New Jersey.
- Gordon, E. A., Henry, E., Louwers, T. J., & Reed, B. J. (2007). Auditing Related Party Transactions : A Literature Overview and Research Synthesis. *Accounting Horizons*, 21(1), 81–102.
- Gordon, E. A., Henry, E., & Palia, D. (2004). Related Party Transactions and Corporate Governance. *Advances in Financial Economics*, 9(04), 1–27. doi:10.1016/S1569-3732(04)09001-2
- Huang, D., & Liu, Z. (2010). A Study of The Relationship between Related Party Transactions and Firm Value in High Technology Firms in Taiwan and China. *African Journal of Business Management*, 4(9), 1924–1931.
- Kohlbeck, M., & Mayhew, B. W. (2010). Valuation of Firms that Disclose Related Party Transactions. *Journal of Accounting and Public Policy*, 29(2), 115–137. doi:10.1016/j.jaccpubpol.2009.10.006
- Kohlbeck Mark & Mayhew Brian. (2004). *Related Party Transactions* (pp. 1 – 40). Madison.



Liong Tong, T. (2012). Chapter 13 :Segment Reporting and Related Party Disclosures. In *Financial Accounting and Reporting in Malaysia* (pp. 992–1000).

MASB. (2013). *Malaysian Financial Reporting Standard 124 Related Party Disclosures* (pp. 733–748). Malaysia.

Munir, S., & Mohd-Saleh, N. (2009). *Related Party Transactions, Family Ownership and Earnings Quality: A Study Of Malaysian Firms* (pp. 1–46). Malaysia.

OECD. Guide on Fighting Abusive Related Party Transactions in Asia (2009). Manila, Philippines: Corporate Governance Series.

Ryngaert, M., & Thomas, S. (2012). Not All Related Party Transactions (RPTs) are the Same: Ex Ante versus Ex Post RPTs. *Journal of Accounting Research*, 50(3), 845–882. doi:10.1111/j.1475-679X.2012.00437.x

Securites Commission Malaysia. Chapter 20 : Special Requirements for Related-Party Transactions. Retrieved October 23, 2013, from <http://www.sc.com.my/wp-content/uploads/eng/html/resources/guidelines/chapter20.html>

Acknowledgements

We acknowledge the Ministry of Education Malaysia for the grant that assists this research (Vote No. 57089).

NUR SHAIDA BINTI MOHD ADNAN
School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA

AKMALIA MOHAMAD ARIFF
Lecturer
School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA



The investigation of the credit risk and its role in cash flows, macroeconomic factors and competition in Iranian banking industry

Yahya Kamyabi

Department of Accounting, University of Mazandaran, Babolsar, Iran

Sahar Ashjar

Nour Branch, Islamic Azad University, Iran.

Abstract

Regarding article 44 of our Constitutional Law about the trend of privatization in Iran, the increase of non-governmental units and their needs for financial resources for more development have been investigated in present research. Thus, conferring credit is highly important in these units. But regarding the fact that a considerable amount of cash resources in Iran are financed through banks and financial entities, the salient problem is considered to be the risk resulting from repayment of these facilities. Therefore, regarding what was pointed out it is clear that the recognition and study of effective factors in credit risk in banks and financial entities and its effect on some indexes such as cash flows' risk, macroeconomic factors, and competition in banking industry is highly important. Below each of these factors will be studied to try to avoid the incurring of losses due to the deficiencies in repayments for the loans and bank crises following that.

Introduction

Many countries have encountered financial crises during the last two decades and following that a considerable number of entities acting in those countries have been forced to stop their activities or restructure. Studies by international banks have shown that the occurrence of the crises mentioned resulted in dissolution of a great amount of financial resources of those countries. The crises mentioned make the importance of identifying the relationship between economic conditions and the safety of



banking system clear because in crisis time the level of non-current claims increases a lot and a considerable amount of banking resources is lost (Espinoza & Prasad, 2010). Currently most banks in Iran face with resource blocks as deferred claims since regarding the trend of increasing the delayed facilities, the facility conferring power of the banks and finally their income making is reduced. Meanwhile, the ratio of non-current claims to facilities has increased to several times as much as average acceptable limit (%2). Ebrahimi and et al (2011) Accordingly the reduction of facilities paid may result in credit risk and finally performance reduction, suitable economic indexes reduction, and competition in market for banks and financial entities reduction will happen (Borhani, 2010).

Credit risk

Risk concept plays a key role in financial markets. Thus, it should be known and measured. Risk is not necessarily a negative phenomenon. There is a risk along with any opportunity and principally we can not remove all risks because if so, all opportunities will be lost either (Carl Olsson, 2002). On the whole the risks that banks and financial entities encounter are often the risk of resource absorption and credit risk and these two risks finally result in bankruptcy in banks. The only important point about resource absorption risk is the importance of decision making about interest rate decided for the deposits and it should be made in a way that there would be the possibility of competition in the market (Dermine, 1986). But the other type of risk, emphasized on more in the present research, is the credit risk and dangers resulting from it. As Hui & et al (2010) believe reduction in operating cash flows gained from facilities, results in main changes in costs of business unit and investments. Also it will result in more sensibility of losses by business unit. According to Gary & et al (2011) credit risk finally results in earning elements' risk and in future will cause the increase of lack of repayments of debts risk and bankruptcy risk and this can create earning management possibility in financial reporting (mbierowicz and Rauch, 2014).

Credit risk and cash flows risk

As it seems that liquidity risk is a reduction cause for earnings, credit risk also affects cash flows risk and results in a reduction in cash flows (Dermine, 1986). In theory, liquidity risk and credit risk should have a positive correlation. This hypothesis was proposed in theoretical financial intermediary contexts such as a model posed by Bryant in 1980 and also Diamond & Dybwig in 1983. The development of these models



showed that risky assets of banks accompany lack of absoluteness and are along with economic liquidity risks (Samartin, 2003; Air & Puree, 2012).

Based on these models, liquidity and credit risks should have a positive relationship and help the inconsistency of banks jointly. The idea of a positive relationship between liquidity and credit risks is supported by a series of new texts which concentrate on fiscal year 2007/2008 either. Some of these texts are: Diamond & Rajan (2005); Acharya & Vis Vantan (2011); Gorton & Metrick (2011); and He & Xiong (2012). Based on the development of Diamond & Rajan's (2001) model, it was found that if many of the economic projects financed through bank loans can not satisfy the demand of depositors, when the value of these assets reduces, more depositors will claim for their money and this is the result of higher credit risk along with higher liquidity risk through depositor's demand.

Another viewpoint about the relationship between liquidity risk and credit risk was posed by Gorton & Metrick (2011). Their experimental analysis showed that in today's guaranteed modern banking against traditional banking and during the recent financial crisis, credit risk in loans not having any support resulted in considerable increases in interest rate in business among local banks. As Acharya & Naqvi (2012) believed, although these researches mostly have focused on certain aspects of liquidity (such as certain assets or deposits) and very specific characteristics of credit risk (such as loan commitments) or they have focused on very specific economic opportunities, there is a positive relationship between credit risk and liquidity risk in a broad perspective and within a set of data about small and medium banks during good economic conditions.

The role of credit risk on factors in macroeconomics

Froyland & Larsen (2002) showed in their study that negative changes in real economy will result in creating losses in loans for financial entities. Kevin & Christopher Metli (2003) tried to analyze the occurrence of the reduction of loans' quality in banking industry during late 1999 to the end of third season in 2002 and investigated about its potential negative effects on industries and overall economy. They compared the problems related to the quality of loans during the period mentioned and the periods of late 1980s and early 1990s, and found out that loans in certain industries such as telecommunication during the period under investigations (late 1999 to third season 2002) and bad macroeconomic cycles had a prominent role in increasing non-current claims. Then Jimenez & Saurina (2005) found out in a study that the ratio of non-current facilities and increase in loan portfolio and economic growth have a



direct relationship. Also during economical boom periods, bond obligations are not taken into consideration seriously, while it is vice versa in regression periods. This was posed as an evidence for weaker credit standards in boom periods.

Hansjorg Lehmann & Micheal Manz (2006) used the data of Swiss banks and tried to identify the effect of macroeconomic variables on banks' profitability. They estimated different elements of bank income on a broad set of macroeconomic variables and some banking characteristics. The results showed that effects of macroeconomic variables on banks' profitability are statistically meaningful. On the other hand, Salas & Saurina (2007) modeled the ratio of non-current loans in the form of a function of macro and micro economics (taken from banks' balance sheets). They found out that the ratio of non-current facilities has a direct relationship with economic growth rate, facilities' growth, size, and capital of the bank. Davern & et al (2008) used a vector self correlation model containing 3 variables of: 'real gross domestic product (GDP)', 'consumer products retail price index (CPI)', and 'interest rate', in order to study the interactions between banking section and macroeconomics in Germany. This model was reinforced by applying GDP of America as an outflow variable in order to consider this fact that German economy is considered as a very important economy in the market and it was thought as a variable showing banking status. Results of their research showed that the ratio of non-current facilities and GDP, CPI, and interest rate have a direct relationship.

Finally Espinoza & Prasad (2010) studied effective factors on non-current facilities in Persian Gulf regions. Results of their research showed that ratio of non-current facilities increases by reducing economic growth. The increase of interest rate results in increasing non-current facilities. Bigger banks and also banks having lower costs have lower non-current facilities' rates. Accordingly, increasing facilities' level results in increasing non-current facilities' level, and it also results in increasing risk acceptance of banks. Therefore, it should be taken into consideration that on the whole increasing credit risk affects factors of macroeconomics negatively.

Credit risk and competition in banking industry

Competitiveness is a process through which every institution tries to act better than others and override them. In international scope, countries should compete with each other due to shortages in financial, technical, and technological resources to achieve wealth and make their people benefit from welfare. Thus, the acquisition of competitive capabilities has changed into one of the basic challenges of different



countries in today's (Namazi & Ebrahimi, 2012). Researches about the effect of credit risk on competition in products' market leads to cash flows sensitivity in a way that competition in product market increases strategic value of cash reservoirs. Therefore, operating cash flows sensitivity results in a potential that can reduce competition in products' market (Giroud & Mueller, 2010: 2011; Guadalupe & Perez-Gonzalez, 2010). On the other hand, in competitive industries where the strategic value of cash resources may be lower, the potential to foster investment would be more. Thus, if credit risk increases in these profit units, it will lead to increase cash flows risk and finally there would be a reduction of competition in products' market (He and Xiong, 2012).

Theoretically a reduction in loan quality is not an unexpected phenomenon. And this reduction is a result of transferring to worse classes such as delayed loans, deferred loans, and dubious loans and this refers to the reduced control of banks' managers (Pannacchi, 1998). However, recent experimental findings have shown that not qualified loans are growing. Many loans were conferred during the period before the crisis and they were so low qualified and banks should have known about their low quality when they carried out the procedure (Gorton, 1995). Additionally, researches have shown that the reduction of loan conferring standards and then increasing credit risk has affected market structure in banking industry and this has led to a reduction in the market for banking industry (Dell Ariccia & et al, 2008).

Conclusion and suggestions

Regarding that credit risk is defined as the probability of not collectability of a claim or an asset, banks potentially encounter credit risk resulted from lack of collection of the original amount or the interest for conferred facilities. Giving higher facilities will result in accepting higher credit risks on the part of banks and this risk is resulted from the probability of deferred payment or loss of a part of those facilities. But identifying the relationship above is more important in financial crisis periods and it results in recognizing the resistance of banking system, specifically regarding the lack of collectability of the facilities paid when banking crises happen. In addition to what was pointed out above, it is necessary to note that one of the most challenging issues for the banking system in our country during some recent years has been the process of transferring claims into non-current classes and this can affect cash flows risk, macroeconomics, and competition in banking industry and result in a reduction in factors fostering macroeconomics and competition in banking industry and increase cash flows risk. This has been changed into a national challenge due to the key role of banks as a monetary and financial markets of the



country and since banks own the main part of liquidity in our country. Accordingly, it is suggested that first the borrowers should be assessed regarding all aspects in order to confer facilities to the costumers and second, by increasing facility level, the expected earnings of banks should get higher in order to compensate for the high credit risk. If the banking system acts freely and the interest rate of facilities is determined in financial markets, banks can compensate for the credit risk resulting from deferred payments of claims. But if interest rate is determined by the government, banks may not have an appropriate alternate to compensate for credit risk.

References

- Borhani, Hamid (2010). Studying the reasons and causes of creating deferred claims and strategies to reduce them. Tehran 21st Conference on Islamic Banking
- Ebrahimi-e-Kordlar, Ali; Aarabi, Mehran (2011). Studying the application of bankruptcy prediction models (Altman, Falmer, Springate, Zimmersky, and Shirata) in predicting the loss of facilities given to firms enlisted in Stock Exchange. *Journal of Accounting and Auditing researches*. No. 12
- Namazi, Mohammad; Ebrahimi, Shahla (2012). Studying the relationship between competitive structure of product markey and stock return. *Journal of financial accounting researches*, Year 2, No. 3
- Giroud, X., Mueller, H., 2011. Corporate governance, product market competition, and equity prices. *Journal of Finance* 66, 563–600.
- Guadalupe, M., Perez-Gonzalez, F., 2010. Competition and Private Benefits of Control. NBER Working Paper.
- Acharya, V.V., Naqvi, H., 2012. The seeds of a crisis: a theory of bank-liquidity and risk-taking over the business cycle. *Journal of Financial Economics* 106, 349–366.
- Born Imbierowicz, Christian Rauch. (2014). "The relationship between liquidity risk and credit risk in banks. *Journal of Banking & Finance* 40. 242–256
- Carl Olsson, (2002), "Risk Management in Emerging Markets ", Pearson Education Limited.
- Dermine, J., 1986. Deposit rates, credit rates, and bank capital: the Klein-Monti model revisited. *Journal of Banking & Finance* 10, 99–114.
- Espinoza & Prasad, (2010), "Nonperforming Loans in the GCC Banking System and their Macroeconomic Effects", IMF Working Paper. wp/10/224
- Froyland, E. and K. Larsen, (2002), "How vulnerable are financial institutions to macroeconomic changes? An analysis based on stress testing", *Economic Bulletin*, 3/2002, pp. 92–98, Norges Bank
- Gorton, G., Metrick, A., 2011. Securitized banking and the run on repo. *Journal of Financial Economics* 104, 425–45



He, Z., Xiong, W., 2012b. Rollover risk and credit risk. *Journal of Finance* 67, 391–429. Holmström, B., Tirole, J., 1998. Private and public supply of liquidity. *Journal of Political Economy* 106, 1–40.

Samartin, M., 2003. Should bank runs be prevented? *Journal of Banking & Finance* 27, 977–1000.

Jimenez, Gabriel & Jesús Saurina, (2005), "Credit cycles, credit risk, and prudential regulation", Banco de España

Kevin J. Stiroh and Christopher Metli, (2003), "Now and Then: The Evolution of Loan Quality for U.S. Banks", Federal Reserve Bank of New York, Volume 9

Gary C. Biddle, Mary L. Z. Ma, Frank M. Song .(2011). The Risk Management Role of Accounting Conservatism for Operating Cash Flows. Faculty of Business and Economics The University of Hong Kong

Hui, K. W., S. Klasa, and E. Yeung. (2010). Corporate Suppliers and Customers and Accounting Conservatism. Working paper, Hong Kong University of Science and Technology.



The Influencing of Local Parliaments (DPRD) Control Function on Good Government Governance (GGG) with their knowledge about budget as a moderating variable (study on local parliaments of Bengkulu Province 2009-2014).

**Filda, Fadli; Isma Coryanata
Maksi-Unib**

1.INTRODUCTION

Background

Council members are actively involved in drafting local regulations (not only approve the draft prepared by the government) and plays an important role in the budgeting process. It also shows the transparency of Parliament to the public to provide input and to control public policy. Transparency is defined in Section 45e of Act No. 32 of 2004 on Regional Government as an obligation to "absorb, accommodate, collect, and follow the aspirations of the people". Other legislation, including Act No. 25 Year 2004 on National Development Planning System and the Act No.10 of 2004 regarding legislation, also providing the legal framework for how members of parliament have to interact with the community. Legislative Council is the regional representative body as an element of the regional administration.

This control function is important for Parliament to be more active and creative in responding to the obstacles to the implementation of the regulation. With the control function of local parliament, the executive as policy implementers will be spared from a variety of fraud, irregularities and fraud. From the results of the supervisory board of an effective, efficient and careful precautions be taken (preventive) or early detection, to improve policies and improving the implementation of the policy.

Examples of corruption are the hottest in the province of Bengkulu in hospital RSUD M.Yunus corruption in disbursement of incentives 20 provincial government officials and members of the Commission IV (team builder hospital) Local Parliament of Bengkulu Province that violates the rules. Alleged embezzlement honor the services of 20 people has been going on since 2010. The corruption case allegedly amounts to billions of rupiahs (Bengkulu Ekspres, Tuesday, March 5, 2013).

So in reality, the role and function of Parliament which had been guaranteed by Act No. 22 of 1999 is not going well. If we look at the news in the mass media, the role and functions of Parliament that occurs in most regions in Indonesia is still far from expectations. As the representative body of the people, should all actions and policies are made in the interest of the people, but the opposite happened. The board members tend to be more selfish, class, and political party than the interests of the people.

So based on the background, the problems and the above phenomenon, the researchers are interested in doing research on the theme : *The Influencing of Local Parliament (DPRD) Control Function of Good Government Governance (GGG is proxied by Accountability, Community Participation, and Public Policy Transparency) with*



their Knowledge about Budget as a Moderating Variable.

Problem Formulation

1. Is Parliament Control Functions influence Accountability?
2. Is Parliament Control Function influence Public Participation?
3. Is Parliament Control Function influence Transparency Public Policy?
4. Is Knowledge of budget moderate the relationship between Parliament Control Function with Accountability ?
5. Is Knowledge of budget moderate the relationship between Parliament Control Functions with Public Participation?
6. Is Knowledge of budget moderate the relationship between Parliament Control Functions with Transparency ?

Research Objectives

1. To provide empirical evidence that the Parliament Control Function influence Accountability.
2. To provide empirical evidence that the Parliament Control Function influence Public Participation.
3. To provide empirical evidence that the Parliament Control Function influence Transparency of Public Policy.
4. To provide empirical evidence that knowledge of the budget moderate the relationship between the Parliament Control Function with Accountability.
5. To provide empirical evidence that knowledge of the budget moderate the relationship between Parliament Control Functions with Public Participation.
6. To provide empirical evidence that knowledge of the budget moderate the relationship between Parliament Control Functions with Transparency Public Policy.

Benefits of Research

The benefits of this research are 1) For the Parliament can be used as input in supporting the implementation of regional autonomy, especially the increase in financial control function of the parliament area. Board members are expected to increase their knowledge about budget . So the Parliament is expected to create programs that contribute to improving the quality and capabilities. 2) For a political party can provide input and reference when recruiting board members and the development of a cadre party. 3) For the Local Government and Communities. For Local Government is expected to be input in supporting the implementation of regional autonomy and to realize Good Government Governance (GGG). For people to be able to monitor and evaluate the performance of Parliament. 4) For the academics are expected to contribute to the development of the Public Sector Accounting literature, especially the development of Management Information Systems in the Public Sector.

Scope of Research

Good Government Governance (GGG) in this study is limited to only three basic principles, namely Accountability, Community Participation, Transparency and Public Policy, as it refers to the study Coryanata (2007) which are the three basic principles of Good Government Governance (GGG) are important. Because knowledge is very broad sense, the knowledge in this study is limited to knowledge and understanding of respondent about RAPBD / APBD with a detailed budget, Budget Calculation Memorandum, General Public Policy Budget (KUA), the Consolidated Statement and Accountability Report Regional Head, the ability to detect if there is waste or failure of the budget and if there is leakage, through knowledge and understanding of the budget draft board / budget in the context of performance-based budget.

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Agency Theory

According to Carr and Brower (2000) and Halim Abdullah (2009), a simple agency models assume two options in the contract: (1) Behavior-based, is the principal must be monitor the behavior of agents and (2) Outcome-based,



namely the existence of incentives for motivate agents to achieve the interests of the principal. The theorists adhered to the proposition that agents behave opportunistically toward principals. Opportunism means that when a partnership exists between the principal and the agent, agent self-interest will most likely occur. According to Abdullah (2004) on government, legislation implicitly a form of contract between the executive, legislative, and public. The regulation stated all obligations and rights of the parties involved in the government.

The role of the Local Parliament (DPRD)

When viewed from the perspective of the role, function, and position of Parliament, the role of Parliament is a set of behaviors that are expected to be members of parliament corresponding job descriptions / duties (Syafwinei, 1995) in Witono (2003) and are actively using rights and obligations to perform tasks and function as a member of the legislature. The role and functions of Parliament will be significant changes in line with the reduction of its authority. With the balance of rights and responsibilities between the executive and the legislature is expected to corruption rife in parliament may decrease with the maturation of democracy in public life. The realization of "Clean and Good Governance" is the hope of all people (Kartiwa: 2006). So the role of containing the rights and obligations which must be an individual in society, the appropriate norm. The role is a function.

Good Government Governance (GGG)

Good Government and Good Governance characterized by three main pillars which are the basic elements that are interrelated (Prajogo, 2001). These three are the basic elements of participation, transparency and accountability. Running of the government must be held in a transparent manner and the implementation of the government must be accountable. In the language of accounting, accountability (ability to provide accountability) are the basis of financial reporting (Wilopo, 2001). The government's financial reporting is an important role in order to fulfill the task of government that is accountable to the public in a democratic society.

The financial statements produced by the government's public sector organizations is the main instrument for creating public sector accountability (Mardiasmo, 2002). Accountability refers to the obligation of an individual, a group or an organization that is assumed to be carrying out the authority and / or compliance responsibilities. Such obligations include:

Answering, attempt to provide an explanation or justification for the implementation and / or compliance responsibilities.

Reporting, reporting the results of the implementation and / or compliance responsibilities.

Producing, assuming liability for the results achieved.

Good governance and clean governance began to surface in Indonesia since the 1990s, especially among the state-aid / loans (donor agency). Good governance and clean government is an aspect that needs to be considered in granting aid / loans good loan (soft loans-small flowers) and grants. The word is derived from the word governance to govern (different meaning with to command or to order) which means the rule. Governance according to UNDP as quoted Mardiasmo (2002) suggests "the way of political, economic, and administrative authority to manage the nation's affairs at all levels". Governance is defined as the implementation of political authority, economic, administration to manage the affairs of the nation.

Accountability

Form of accountability by Krina (2003) as follows:

Decisions must be made in writing and available to every citizen in need.

The accuracy and completeness of the information.

Explanation policy objectives are taken and communicated.

Feasibility and consistency.

Dissemination of information regarding a decision.



Public Participation

According Krina (2003) participation goal is a demand from the public for them to be empowered, given the opportunity, and are included to play a role in the bureaucratic processes ranging from planning, implementation and control of public policy. According Krina (2003) forms of participation are:

The involvement of officials through the creation of value and commitment.

The existence of a forum to accommodate participation.

Community involvement in the decision-making process.

The focus of the government is to provide direction and invite others to participate and know the forum, meetings with community groups (musrenbang) relating to the planning and implementation of the financial management area. The focus of the government in this case is to provide direction and invite others to participate.

Access for the public to express their opinions in the decision-making process.

Transparency of Public Policy

The goal of transparency is to provide financial information that is open to the public in order to realize good governance. According Krina (2003) forms of transparency are:

The provision of clear information about procedures, costs, and responsibilities.

Ease of access to information.

Constructing a complaints mechanism.

Improving the flow of information.

Knowledge about Budget

Yudhoyono (2002) in Coryanata (2007) states that the Council will be able to use their rights properly, duties and obligations effectively and proportionately put position if each member has sufficient knowledge in the technical conception of governance, public policy and so on . Knowledge that will be needed in the area of financial control one of which is the knowledge of the budget. If knowledge about budget better than expected councilors to detect the presence of wastage and leakage. Experience and high knowledge would greatly help a person in solving the problems that it faces in accordance with the position as a member of parliament as representatives of the people.

The Concept of Public Sector Budget

Budget is an important tool for controlling and planning of an organization (Anthony and Govindrajana, 2004). Budget is one of the main important component in the planning, which contains plans for future operations and indicates the activities to achieve organizational goals (Hansen and Mowen, 2003). Management control is a must in any organization to provide assurance that the strategy of the organization is carried out effectively and efficiently. Management control is the process by which managers affects all parties within the organization to implement the organization's strategy (Anthony and Govindrajana, 2004). According to Robinson (2006) in an effort to improve the quality of public accountability, the implementation of performance budgeting approach (performance-based budget) be considered the best option at this time. By using the performance approach each budget value (input) must be connected to the results to be obtained in the form of output and the results (outcomes). Budget Country / Region Budget that is presented annually by the executive, provide detailed information to the DPR / DPRD and the public about what programs are planned by the government to improve the quality of people's lives, and how the programs are funded.

Budget Cycle

According Mardiasmo (2009) the basic principles of the budget cycle needs to be known and well understood by government administrators. Basically the principles and mechanisms of relative budgeting did not differ between the private sector and the public sector (Henley et al, 1990). Budget cycle includes four stages



consisting of:

Budget preparation phase (preparation).

Budget ratification phase (approval / ratification).

Budget implementation / execution of the budget (implementation).

The Purpose of the Public Sector Budgeting

1. Helping government achieve fiscal goals and improve coordination between divisions within the government.
2. Helps create efficiency and fairness in providing public goods and services through the prioritization process.
3. Allows for the government to meet the spending priorities.
4. Increase the transparency and accountability of government to Parliament and the public.

Hypothesis:

H1: Local Parliament Control Function significant effect with Accountability.

H2: Local Parliament Control Function significant effect with Public Participation.

H3: Local Parliament Control Function significant effect with Transparency of Public Policy.

H4: Knowledge about budget moderate the relationship between Parliament Control Function with Accountability.

H5: Knowledge about budget moderate the relationship between Parliament Control Function with Public Participation.

H6: Knowledge about budget moderates the relationship between Parliament Control Function with Transparency of Public Policy.

Theoretical Framework

From the description of the theoretical study and the development of hypotheses that have been described above, the relationship between variables can be described in terms of a theoretical framework in Figure 1 this:

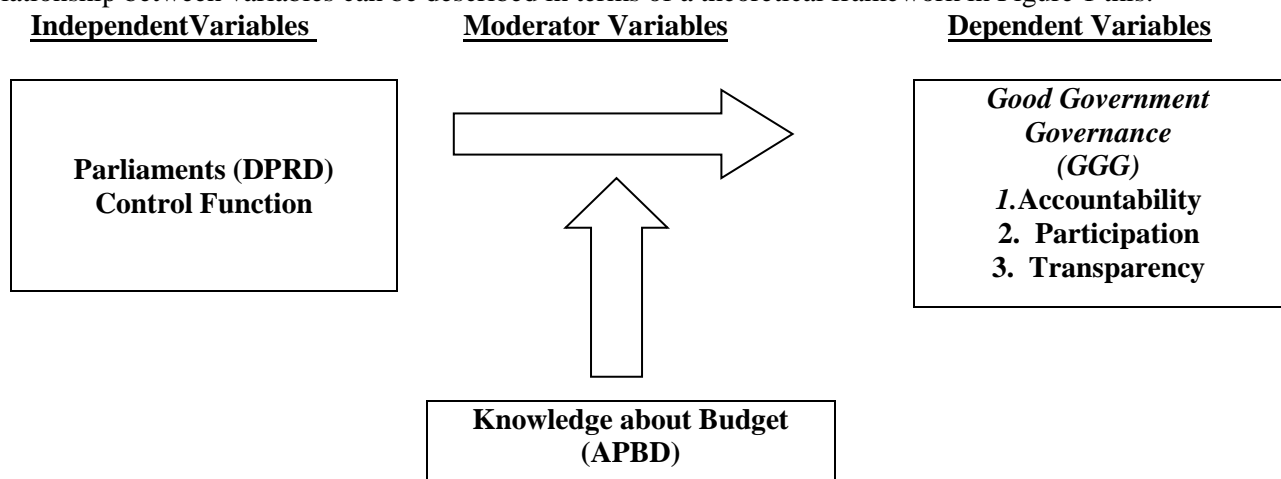


Figure 1

Model of the Influencing of Local Parliaments (DPRD) Control Function on Good Government Governance (GGG) with their Knowledge about Budget as a Moderating Variable

3. METHODS

Sampling Method

The population in this study is a member of the Local Parliament of Bengkulu Province. The sample was all local parliament members of Bengkulu Province totally 45 people. So the sample size is 45 people, so the number of



copies of the questionnaires were 45. Submission of the questionnaire in this study with the hope of respondents can answer questions based on the experience in the control of budgets ranging from preparation, ratification, implementation, reporting and evaluation (focused on Ratification, Reporting, and Evaluation Phase).

The data used in this study is primary data obtained directly from questionnaires to be filled of the respondents in the Local Parliament Members of Bengkulu Province. The data was collected by distributing questionnaires are accepted directly to the respondents to be filled, until the return is taken alone to the respondent in accordance with promised. The processed data is an accepted data from the questionnaires were returned and completed.

Operational Definition and Measurement of Variables

1. The independent variable is Local Parliament Control Function.
2. The dependent variable is the Good Government Governance (which is proxied by the Accountability, Public Participation, and Transparency Public Policy).
3. The moderating variable, namely Knowledge about Budget.

According Sugiyono (2011), the moderating variables are variables that influence (weaken or strengthen) the relationship between the dependent and independent variables. All calculations and statistical analyzes performed with SPSS software (Statistical Package for Social Science) for Windows version 18.0.

Data Analysis Techniques

Data analysis techniques in this study is to use the regression model. In one study, the possibility of problems in the regression analysis is quite often in the match prediction model into a model that is inserted into the data set. This study tested with several statistical test which consists of test the quality of the data, descriptive statistics, and hypothesis testing.

Test Data Quality

According Ghozali (2011) there are two concepts to measure the quality of data that is reliability and validity. The quality of the data generated from the use of the instrument can be evaluated through validity and reliability. The testing of each to determine the consistency and accuracy of data collected from the use of the instrument. In other words, the test aims to determine whether the instruments used are valid and reliable, because the truth of the processed data will determine the quality of research results. In this study to measure the quality of data used, among others:

Test Validity

Validity test aims to measure the quality of the instruments used, and indicates the level of validity or the validity of an instrument, as well as how well a concept can be defined by a measure. Instrument as valid if it is able to measure what is desired and disclose data appropriately investigated. Tests carried out using factor analysis (factor analysis). To measure the degree of relatedness (intercorelations) between the variables and the appropriateness of the factor analysis is the Kaiser-Meyer-Olkin Measure of Sampling Adequacy (KMO-MSA) (Hair et al., 1998). The data analysis can be done when the Kaiser's MSA factor above 0.5 and items included in the factor analysis are the items that have a factor loading of more than 0.3 (depending on the number of samples) in Ghozali (2011).

Test Reliability

Reliability test is performed by calculating Cronbach alpha to test the feasibility of the consistency of the whole scale is used. Said to be reliable if the instrument has a Cronbach alpha of more than 0.7.

Test Model

1. Simple Regression Analysis



Used to test hypotheses 1, 2 and 3 that the regression equation can be formulated as follows:

$$Y = \alpha + \beta_1 X_1 + e$$

Description: Y = Good Government Governance (GGG)
 α = constant
 β_1 = regression coefficient.
 X_1 = control function

2. Residual Test

Steps in Residual Test :

1. Regressed control function variables (X_1) with knowledge variables (Z), then get the residual value.

$$Z = \alpha + \beta_1 X_1 + e$$

Description: Z = Knowledge
 α = constant
 β_1 = regression coefficient
 X_1 = Control Function

2. Regressed each variable of GGG (proxied by Accountability, Participation, and Transparency) with Absolute Residuals obtained from step 1.

$$(\text{Absolute Residual}) = \alpha + \beta_1 X_1 + e$$

Description: α = constant
 β_1 = regression coefficient
 X_1 = Good Government Governance (GGG).

4. RESULTS AND DISCUSSION

Return Questionnaire

Questionnaires were distributed as much as 46 questionnaires, but of the 46 questionnaires distributed were only 38 or 82.61% of the questionnaires were returned. So the response rate of the respondents in this study was 82.61%.

Data Response Rate clearly can be seen in Table 4.1 below:

Table 4.1
Response Rate Data

The number of questionnaires distributed	46 questionnaires	100 %
The questionnaires were returned	38 questionnaires	82,61 %
The questionnaires were not returned	8 questionnaires	17,39 %
The questionnaire can not be processed	6 questionnaires	13,04 %
The questionnaire used in the study	32 questionnaires	69,56 %

Source: Primary Data Processed, 2013



Profile of Respondents

Table 4.2 below shows information regarding gender, age, education and whether or not the respondent has ever been a member of the previous parliament.

Tabel 4.2
Profile of Respondents

Note	Quantity	Percentage
Gender		
- Male	26	81,25 %
- Female	6	18,75 %
Totally	32	100 %
Age		
- 20-30 years old	1	3,13 %
- 31-40 years old	7	21,87 %
- 41-50 years old	17	53,13 %
- > 50 years old	7	21,87 %
Totally	32	100%
Education		
- D3	1	3,13 %
- S1	20	62,50 %
- S2	11	34,37 %
Totally	32	100%
Has been a member of Local Parliament (DPRD)		
- Ever	16	50 %
- Never	16	50 %
Totally	32	100%

Source: Primary Data Processed, 2013

Descriptive Statistics

The measurement results of the descriptive statistics of research variables (control function, accountability, participation, transparency, and knowledge of the budget) using descriptive statistics table that shows the number of theoretical range, the average of theoretical, the actual range (real), mean, and standard deviation can be seen in Table 4.3 as follows:

Tabel 4.3
Descriptive Statistics

Variables	N	Theoretical Range	Average of Theoretical	Actual Range (Min-Max)	Mean	Standart Deviation
CONTROL FUNCTION (X)	32	18-90	54	66-88	77,59	7,34
ACCOUNTABILITY (Y1)	32	5-25	15	16-25	21,78	2,35
PARTICIPATION (Y2)	32	7-35	21	24-35	29,34	3,43



TRANSPARENCY (Y3)	32	5-25	15	17-25	19,66	2,03
KNOWLEDGE (Z)	32	15-75	45	54-74	63,03	6,29
Valid N (listwise)	32					

Source: Primary Data Processed, 2013

Based on the above, the respondents answer to each of the variables shown to provide information that all variables (control function, accountability, participation, transparency, and knowledge) tend to be categorized as "good". This is indicated by the actual range value of all variables higher than the average of theoretical of each variable. Mean all variables higher than the average of theoretical for each variable. It means most respondents gave answers to the scale of 4 ("agree") on each question item.

Validity Test Data

The results of validity test data with a significant value of KMO-MSA test and Bartlett's Test of Sphericity can be seen from Table 4.4 below:

Tabel 4.4
Validity Test Data Results

No.	Variables	KMO-MSA	Significant (Bartlett's Test)	Notes
1	CONTROL FUNCTION	0,888	0.000	Valid
2	ACCOUNTABILITY	0,716	0.000	Valid
3	PARTICIPATION	0,775	0.000	Valid
4	TRANSPARENCY	0,682	0,001	Valid
5	KNOWLEDGE	0,846	0,000	Valid

Source: Primary Data Processed, 2013

The results of testing the validity of data to variable Control Function, Participation, Transparency, and the Knowledge indicates all values of KMO-MSA > 0.5. So all of these variables are valid.

Reliability Test Data

According Ghozali (2011), variables or constructs research said to be reliable if the value of the Cronbach Alpha (α) > 0.7. Increasingly alpha value close to 1 then the reliability of the data is more reliable. Results of reliability test data can be seen in Table 4.5 below:

Table 4.5
Reliability Test Data Results

No.	Variables	Cronbach's Alpha Value	Notes
1	CONTROL FUNCTION	0,905	Reliable
2	ACCOUNTABILITY	0,836	Reliable
3	PARTICIPATION	0,874	Reliable
4	TRANSPARENCY	0,711	Reliable
5	KNOWLEDGE	0,875	Reliable

Source: Primary Data Processed, 2013



From Table 4.5 above shows that all the variables are reliable. This can be seen from all the values of Cronbach Alpha (α) > 0.7.

Hypothesis Testing

Hypothesis Testing 1, 2 and 3

The following Table 4.6 presents a summary of the results of testing a simple linear regression to test hypotheses 1, 2, and 3 as follows:

Table 4.6
Results of Hypothesis Testing 1, 2, 3

Models	Regression Models	Beta Coefficient		t	Sig t	R ²	F	Sig F	NOTES
		Constanta	X						
Model I	$Y_1 = \alpha + \beta X$	-7.474E-17	0.598	4.084	0.000	0.357	16.678	0.000	SIGNIFICANT
Model II	$Y_2 = \alpha + \beta X$	-5.047E-17	0.559	3.697	0.001	0.313	13.667	0.001	SIGNIFICANT
Model III	$Y_3 = \alpha + \beta X$	-9.904E-19	0.223	1.250	0.221	0.050	1.563	0.221	NOT SIGNIFICANT

Source: Primary Data Processed, 2013

These results support the hypothesis testing hypotheses 1 and 2, that the control function significant effect on accountability and public participation. However, these results do not support the hypothesis testing 3, that the control function does not significantly influence the transparency of public policy.

Testing Hypothesis 4,5, and 6

To test this hypothesis used the residual test of the third GGG proxies namely accountability, participation, and transparency. The summary of the test results to test the hypothesis 4,5,6 residuals can be seen in Table 4.7 below:

Table 4.7
Results of Hypothesis Testing 4,5,6

Models	Regression Models	Beta Y Coefficient	Sig t	Conclusions
MODEL I	(Absolut Residual) = $\alpha + \beta Y_1 + e$	-0.173	0.008	MODERATE
MODEL II	(Absolut Residual) = $\alpha + \beta Y_2 + e$	-0.149	0.025	MODERATE
MODEL III	(Absolut Residual) = $\alpha + \beta Y_3 + e$	-0.068	0.322	NOT MODERATE

Source: Primary Data Processed, 2013



These results support the hypothesis testing hypotheses 4 and 5, that the Knowledge of Budget moderate the relationship between the Local Parliament Control Function with Accountability and Public Participation. However, these results do not support the hypothesis testing 6, that the Knowledge of Budget does not moderate the relationship between the Local Parliament Control Function with Transparency of Public Policy.

Discussions

The influencing of Local Parliament Control Function on Accountability

Based on the results of testing hypothesis 1 it can be concluded that the Local Parliament Control Functions significant effect on Accountability. Significant effect in this context means more better the Local Parliament Control Function so the better of the quality of Accountability. The results are consistent with research Wardayani (2010) that the role of Parliament in the area of financial control is very large and has a strategic value to be able to control the region's financial policies are economically, efficciently, effectively, transparent, and accountable, although in fact there are problems and weaknesses in the financial management area (by the local government / executive). The results of this study also supports research Coryanata (2007), Pramita and Andriyani (2010), Utomo (2011), Mayasari (2012), and Solikin (2011).

The influencing of Local Parliament Control Function on Public Participation

Based on the results of testing hypothesis 2 can be inferred that Local Parliament Control Functions significant effect on Public Participation. That is the better Local Parliament Control Function the better Public Participation. The results of this study support the results of research conducted by Coryanata (2007) that the Public Participation (as a moderating variable) influence the relationship between knowledge about the budget council with oversight of public financial budget significantly.

The influencing of Local Parliament Control Function on Transparency of Public Policy

Results of testing hypothesis 3 Local Parliament Control Function concluded that no significant effect on Transparency of Public Policy. The results of this study support the results of research conducted by Mayasari (2012), namely the transparency of public policy does not affect the quality of the relationship with the supervisory board members budget. Research Sopanah (2003) proved that the interaction between the knowledge of the budget and transparency of public policy does not significantly influence the control function of the local financial (budget). Transparency of public policy is still in its early stages of implementation are still in the rhetoric and formality. Access to public policy is difficult and only certain people who can get it. However, these results differ from studies Utomo (2011) and Wardayani (2010).

Knowledge of budget moderate the relationship between Local Parliament Control Function with Accountability

Results of testing hypothesis 4 with the residual test proves that the knowledge of the budget moderate the relationship between the Local Parliament Control Function with Accountability. This means that knowledge of the budget that the better and it will strengthen the relationship between the Local Parliament Control Function with Accountability. .

Knowledge of budget moderate the relationship between Local Parliament Control Functions with Public Participation

Based on the results of testing hypothesis 5 it can be concluded that the knowledge of the budget moderate the relationship between Parliament Control Functions with Public Participation. This means that knowledge of the budget will better if the relationship between Parliament Control Functions with Public Participation will strengthen. The effectiveness of Parliament Control Function provide greater opportunities for public to participate in the management of good government governance (GGG). Public participation in policy-making process in any public is important as a respect the principles of democracy in a country (Dwiyanto, 2008). The results of this study support to the research of Indriani (2002), Sopanah (2003), Coryanata (2007) and Basri (2008) which public



participation moderate the relationship between knowledge of budget with financial control area.

Knowledge of budget does not moderate the relationship between Local Parliament Control Functions with Transparency

Results of testing hypothesis 6 concluded that knowledge of budget does not moderate the relationship between Local Parliament Control Functions with Transparency. So the knowledge variable is not a variable that moderates the relationship between Control Function variable with Transparency variable, because of the residual test results do not prove to be a moderating variable. Then the knowledge of the variables in the context of the budget is likely to be appropriate or consistent with previous research by Indriani (2002) as the independent variable.

However, overall test results support the hypothesis 4,5,6 stating that knowledge about budget moderate the relationship between Parliament Control Functions with good government governance (GGG). Therefore, 4,5,6 hypothesis are accepted. These results are supported by research of Indriani (2002), Coryanata (2007), Wardayani (2010), and Palupi (2012).

5. CLOSING

Conclusions

1. Local Parliament Control Functions significant effect on Accountability. This suggests that the higher of Local Parliament Control Functions make Accountability the better.
2. Local Parliament Control Functions significant effect on Public Participation. This suggests that the higher of the Local Parliament Control Functions make Public Participation the better.
3. Local Parliament Control Functions no significant effect on Transparency of Public Policy. This indicates that transparency is still the domain of the executive. Communities and stakeholders, demanding the government to open up access to the widest governance practices. In making public policy, for example, the public demanded that the government not only to be more open, but also involve stakeholders in the process of public policy making.

Overall goals should the hypothesis tests 1,2, and 3 stating that Local Parliament Control Functions significant effect on Accountability, Public Participation, and Transparency is acceptable.

4. Knowledge of budget moderate the relationship between Local Parliament Control Functions with Accountability. This suggests that the higher knowledge of the budget it will further strengthen the relationship between Local Parliament Control Functions with Accountability.
5. Knowledge of budget moderate the relationship between Local Parliament Control Functions with Public Participation. This suggests that the higher knowledge of the budget will further strengthen the relationship between Local Parliament Control Functions with Public Participation.
6. Knowledge of budget does not moderate the relationship between Local Parliament Control Functions with Transparency. This indicates that knowledge variable is not moderate the relationship between Local Parliament Control Function variable with Transparency variable, because of the residual test results do not prove to be a moderating variables. Budget information and rationality about policy and rationality, so far is difficult to obtain stakeholders. All public information domain is still bureaucratic and political elite. Although board members have been equipped with adequate knowledge about the budget, but can not do much if the members of local parliament own difficulties in accessing public information that is important, and affects the lives of many people. So it is very difficult to do it.

Overall goals should the hypothesis tests 4,5,6 stating that knowledge of budget moderate the relationship between Parliament Control Functions with Good Government Governance (GGG) is acceptable.

Research Implications

Based on empirical evidence found from the above results the implications for all members of the House of Representatives/Local Parliament (DPRD) of Bengkulu Province is very important and urgent. Strengthening of



Local Parliament Control Functions, Budget Functions, and Legislation Functions, the importance and urgency of strengthening to immediately realize the Good Government Governance (GGG) is proxied by accountability (accountability in the implementation of both the institution itself and in Local Parliament and Local Government), immediately realizing Participation, and Transparency. As well as the importance and urgency of strengthening to improve the knowledge of the Budget for all members of the Local Parliament (DPRD) of Bengkulu Province. Strengthening the Local Parliament Control Functions will be able to reduce the disease KKN (corruption, collusion, and nepotism) among institutions of governance (Local Government) and the Parliament itself. So the effective and efficient control has implications for the establishment of mutual relations (checks and balances) between the legislative, executive, and civil society.

Found empirical evidence from this study have implications for the development of Public Sector Accounting literature especially for Management Control Systems in public sector. It also shows an empirical evidence that the Local Parliament Control Functions significant effect on Accountability and Public Participation. However Local Parliament Control Functions do not significant effect on Transparency of Public Policy. Knowledge of Budget moderate the relationship between the Local Parliament Control Functions on Accountability and Public Participation. But knowledge of the Budget does not moderate the relationship between Local Parliament Control Function with Transparency Public Policy.

Limitations of Research

1. Respondents used in this study is Local Parliament Members of Bengkulu Province 2009-2014 period, so that conclusions can not be generalized to other settings or overall conditions in Indonesia.
2. Duration of the study is influenced by the difficulty researchers encounter Local Parliament Members of Bengkulu Province (as respondents), because of busy and they are very solid mobility.

Research Recommendations

1. Based on the discussion, conclusions and implications for research on Control Function Variable, Accountability Variable, Participation Variable, Transparency Variable and Knowledge of the Budget Variable, then the suggestions of researchers is need for Strengthening the Local Parliament Control Functions, also need strengthening parliament the other two functions, namely Strengthening Legislation Function and reinforcement Budget Function optimization in order to create the role and functions of parliament for the creation of Good Government Governance (GGG) on local government. The necessity of strengthening unity-gain and intention, determination and action with intelligent breakthroughs to immediately realize the Good Government Governance (GGG) in the province of Bengkulu, which is proxied by Accountability (accountability in the implementation of both the institution itself and in Parliament Local Government), immediate reinforcement to realize Participation and Transparency. As well as the importance and urgency of strengthening to improve the knowledge of the budget for all members of the Local Parliament (DPRD) of Bengkulu Province.
2. Subsequent research is expected to expand the scope of research in order to allow generalized research results in general. Example: There needs to be further research on the Function of Legislation and the Function of Budgeting on Local Parliaments of Bengkulu Province and Bengkulu Regency / City.



REFERENCES

- Abdullah, Syukriy. (2004). Perilaku oportunistik legislatif dalam penganggaran daerah: Pendekatan principal-agent theory. Makalah disajikan pada Seminar Antarbangsa di Universitas Bengkulu, Bengkulu, 4-5 Oktober 2004.
- Anthony, R.N. dan V. Govindarajan. (2004). *Management Control Systems*, Eleventh Edition, McGraw-Hill Companies, Inc, U.S.A.
- Basri, Yesi Mutia. (2008). Pengaruh Pengetahuan Dewan tentang Anggaran pada Pengawasan Keuangan Daerah di Provinsi Riau dan Kota Pekanbaru. *Jurnal Ilmu Administrasi Negara*. Vol.8. No.1, Januari 2008, hal 29-39.
- Bengkulu Ekspres. (2013), 5 Maret. 2 Mantan Dirut RSMY Calon Tersangka. Tersedia di Web : www.bengkuluekspres.online (TKP beonline).
- Coryanata, Isma (2007). Akuntabilitas, Partisipasi Masyarakat dan Transparansi Kebijakan Publik sebagai Pemoderating Hubungan Pengetahuan Dewan tentang Anggaran dan Pengawasan Keuangan Daerah (APBD), Makalah disajikan pada SNA X Makassar, Juli 2007.
- Dwiyanto, Agus, (Editor).(2008). *Mewujudkan Good Governance Melalui Pelayanan Publik*, Cetakan Ketiga, JICA & Gadjah mada University Press, Yogyakarta.
- Ghozali, Imam. (2005) . *Aplikasi Analisis Multivariate dengan Program SPSS*. Edisi 3.Badan Penerbit Universitas Diponegoro. Semarang.
- _____. (2011). *Aplikasi Analisis Multivariate dengan Program IBM SPSS 18*. Cetakan 5. Edisi 1. Badan Penerbit Universitas Diponegoro. Semarang.
- Halim, Abdul dan Syukriy Abdullah (2009). Hubungan dan Masalah Keagenan di Pemerintahan Daerah : (Sebuah Peluang Penelitian Anggaran dan Akuntansi). *Jurnal Akuntansi Pemerintah*. Tersedia di Web : <http://www.bppk.depkeu.go.id/>
- Hansen, Don R. dan M.M. Mowen. (2003). *Management Accounting*. 6th Edition, South-Western College Publishing.
- Indriani, Rini. (2002). *Pengaruh Pengetahuan dan RPPs (Rules Procedures and Policies) terhadap Peranan DPRD dalam Pengawasan Anggaran (Studi Kasus pada DPRD Se-Provinsi Bengkulu)*, Tesis Program Pasca Sarjana Magister Sains Akuntansi Universitas Gadjah Mada, Yogyakarta (tidak dipublikasikan).
- Kartiwa, H.A.(2006). Implementasi Peran dan Fungsi DPRD dalam Rangka Mewujudkan “Good Governance”. *Artikel*. Fakultas Ilmu Administrasi Publik-FISIP UNPAD. Bandung.
- Krina.P, Loina Lalolo. (2003). *Indikator dan Alat Ukur Prinsip Akuntabilitas, Transparansi dan Partisipasi*. Tersedia di Web: <http://www.goodgovernance.com>
- Mardiasmo.(2001). “Pengawasan, Pengendalian, dan Pemeriksaan Kinerja Pemerintah Daerah dalam Pelaksanaan Otonomi Daerah”. *Jurnal Bisnis dan Akuntansi*. Vol.3, Agusuts, hal.441-456.
- Mardiasmo. (2002). *Akuntansi Sektor Publik*, Andi , Yogyakarta.



- _____. (2009). *Akuntansi Sektor Publik*, Andi , Yogyakarta.
- Mayasari, Rosalina Pebrica .(2012). Pengaruh Kualitas Anggota Dewan terhadap Pengawasan APBD dengan Tata Pemerintahan yang Baik sebagai Pemoderating. *Jurnal Ekonomi dan Informasi Akuntansi (JENIUS)*.Vol.2 No.1 Januari 2012.
- Palupi, Nimas Ayu. (2012). Pengawasan Keuangan Daerah dengan Akuntabilitas dan Partisipasi Masyarakat sebagai Moderasi. *Jurnal Universitas Negeri Semarang*.
- Prajogo. (2001). Perspektif Pemeriksa terhadap Implementasi Standar Akuntansi Keuangan Sektor Publik. *Jurnal Akuntansi dan Keuangan Sektor Publik. Kompartemen Akuntan Sektor Publik Ikatan Akuntan Indonesia*. Vol. 02 No. 02. Agustus. pp. 1 – 8.
- Pramita, Yulinda Devi dan Lilik Andriyani (2010). *Determinasi Hubungan Pengetahuan Dewan tentang Anggaran dengan Pengawasan Dewan pada Keuangan Daerah (APBD) (Studi Empiris pada DPRD Se-Karesidenan Kedu)*. Makalah disajikan pada SNA XIII Purwokerto, 2010.
- Robinson, (2006). *Pengaruh Kualitas Anggaran terhadap Efektivitas Pengawasan Anggaran : Pengetahuan tentang Anggaran sebagai Variabel Moderating (Studi Empiris pada DPRD Kabupaten/Kota Se-Provinsi Bengkulu)*. Tesis Program Pasca Sarjana Magister Sains Akuntansi Universitas Diponegoro. Semarang.
- Solikin, Ikin (2011). Pengaruh Penerapan Akuntansi Pemerintahan, Kualitas Informasi Akuntansi dan Kualitas Aparatur Pemerintah Daerah terhadap *Good Government Governance* dan Implikasinya terhadap Kinerja Keuangan (Survey pada Pemerintah Kota dan Kabupaten di Provinsi Jawa-Barat).*Jurnal*. Disertasi. Universitas Pendidikan Indonesia. Bandung. Tersedia di <http://www.univpancasila.ac.id>
- Sopannah, Isa Wahyudi (2003). Pengaruh Akuntabilitas Publik, Partisipasi Masyarakat dan Transparansi Kebijakan Publik terhadap Hubungan Antara Pengetahuan Anggaran dengan Pengawasan Keuangan Daerah (APBD),Makalah disajikan pada SNA VI Surabaya, Oktober 2003.
- Sugiyono. (2011). *Metode Penelitian Kuantitatif, Kualitatif, dan R&D*. Cet.14. Alfabeta. Bandung.
- Utomo, Hari .(2011). *Determinasi Hubungan Pengetahuan Dewan tentang Anggaran dengan Pengawasan Dewan pada Keuangan Daerah (APBD)(Penelitian pada DPRD Jawa-Tengah)*. Tersedia di <http://www.eprints.undip.ac.id>
- Wardayani. (2010), *Pengaruh Pengetahuan Dewan tentang Anggaran, Partisipasi Masyarakat dan Transparansi Kebijakan Publik terhadap Kinerja DPRD dalam Pengawasan Keuangan Daerah dengan Komitmen Profesional sebagai Variabel Moderasi*. Tesis Sekolah Pascasarjana Universitas Sumatera Utara (USU), Medan.
- Wilopo. (2001). Faktor-faktor yang Menentukan Kualitas Audit pada Sektor Publik/ Pemerintah. *Ventura*. STIE Perbanas Surabaya. Vol. 4 No.1. Juni. pp. 27 – 32.
- Witono, Banu (2003). Optimalisasi Peran DPRD dalam Pengawasan Keuangan Daerah. *Jurnal Akuntansi dan Keuangan*. Vol.2, No.2, September 2003, hal 151-168.



World Bank.(1997). *World Development Report, 1997 : The State in the Changing World*. Oxford University Press. Oxford.

World Bank (2000). *Anticorruption in transition: a contribution to the policy debate*. World Bank Publications. p. 40. ISBN 0821348027, 9780821348024. Tersedia di Web : ieg.worldbankgroup.org/grpps.



Discharging Accountability through Governance: Cases from Waqf Institutions in Indonesia

NATHASA MAZNA RAMLI¹

NURUL AINI MUHAMED

NURUL HUSNA MOHD SALLEH

MUHAMMAD FEBRANSYAH

MUHAMMAD MAJDY AMIRUDDIN

Faculty of Economics and Muamalat,

Universiti Sains Islam Malaysia (USIM),

71800 Bandar Baru Nilai, Negeri Sembilan,

MALAYSIA

Abstract

The focus of this study is to examine the governance of waqf institutions in Indonesia. This study focuses on how accountability in waqf institutions are being discharge through governance process. In Indonesia, most of *waqf* is managed by private institutions. As these institutions are amongst Islamic institution, they have played a vital support to the development of the Islamic communities. Prior studies has highlighted that transferring the management of *waqf* to an independent board or body will help to manage *waqf* assets in a professional manner. Data of the study were collected through interview of two *waqf* foundations in Indonesia. The study highlights the governance process of these two foundations. Findings from the study could extend the knowledge in these area and assist in improving *waqf* administrations, particularly in Indonesia.

Keywords: *Waqf*, *waqf* institutions, governance, accountability

¹ Corresponding author can be contacted at: nathasa@usim.edu.my

This research is part of a research under the grant USIM/RAGS/FEM/36/50413



1. INTRODUCTION

Waqf, which is also known as Islamic trust or Islamic endowment is one of the most important institutions that have contributed immensely to the socio-economic and social development since the early days of Islam. *Waqf* can be defined as retaining certain property with the intention of using the benefits for philanthropy act, where there is prohibition of *waqf* assets usage outside of its righteous purposes (Dahlia Ibrahim and Hasnidar Ibrahim, 2013). Cajee (2008) stated that there are growing interest and awareness in *waqf* institutions as one of the tools for the development of community. Indeed, new and modern *waqf* management has put greater emphasize on the principles of accountability and transparency (Cajee, 2008).

The revival of *waqf* institution creates the needs for developing a good governance framework, which could improve transparency and accountability of the institution. The purposes of *waqf* are to provide continuous charity that could generate perpetual income flow for the needy. If good governance is in place, the accountability can be discharge to various stakeholders such as *waqif* (giver) and beneficiaries.

With the establishment of *waqf* institutions, the role of *waqf* in serving society is the main question as many of them is not utilize in providing social services to Muslim society. Moreover, in some Muslim country, *waqf* properties, have been neglected and therefore it is not surprising if some of the *waqf* properties are not recorded properly or some have gone missing. This sort situation has called for a better governance for the institutions to encourage their accountability as a *Nazir* (Person responsible in managing *waqf*) in managing the *waqf* assets.

Ihsan, Ayedh and Shahul (2006) and Cajee (2008) have highlighted that the *waqf* development in the future will largely depend on the good governance of *waqf* institution. In addition, Tunku Alina Alias (2012) stated that the directors of *waqf* should be guided by a Code of Governance, and possibly a Code of Ethics. Thus, the directors and trustees would understand their role, ensure the purpose of *waqf* is delivered, effectively working in *shura* (consultative committee), exercise control over the *waqf* assets and behave with integrity and accountability. Masruki, R. and Shafii, Z. (2013) also stated that *waqf* institution need to established a Professional Code of Conduct and a Code of Ethics for *Mutawalli* (trustee), the management and the workers of *waqf* financial industry towards enhancing their accountability. A sound governance system should be in place so that accountability can be discharge to various stakeholders such as *waqif* (giver) and beneficiaries. Thus, this study concern focus on how the principle of accountability can be achieved through governance process by examining two *waqf* institutions in Indonesia.

The rest of the paper is organized as follows. The next section provides background of *waqf* followed by a discussion on accountability. Section 4 discuss on governance and its relation with accountability while section 5 provide the research objective and design of the study. Section 6 and 7 provides the profile of the *waqf* institutions and research findings and discussion, respectively. The paper concludes in Section 8.



2. LITERATURE REVIEW

2.1 BACKGROUND OF WAQF

Waqf is one of Islamic economic instruments to promote the distribution of public wealth. This perpetual voluntary charity concept is that the underlying asset should remain and the people can take the benefits of the asset. As in the past, the *Waqf* sector has the potential to become part of a strong civil society which promotes socio-economic welfare and reduces inequality. Since the *Waqf* assets should be in existence in perpetuity, the assets must be managed and administered by the appropriate parties responsible to supervise *Waqf* property benefits so that the benefits can be distributed to the recipients.

The charity and alms giving activities are highly appreciated and thus encouraged in Islam. It is understood that *waqf* is one type philanthropic activities in Islam, the same with *zakat* and *sadaqah*. Differently from *zakat* that is compulsory, other types of philanthropic activities (such as *sadaqah* and *waqf*) are encouraged. The perfection of Islam is shown with these great elements of worship. All Muslims activities should be beneficial to society and be directed to get blessing from Allah SWT. In that case, Muslims also should put aside of their asset for the sake of *ummah*, something that they appreciate and valuable. The assets can be in many forms. The *Quranic* versus in Surah al-Imran is among many verses that indicate the encouragement of the philanthropic activities.

By no means shall you attain al-birr (virtue, righteousness), unless you spend (in Allah's cause) of that which you love; and whatever of good you spend, Allah knows it well (Qur'an: 3:92).

In general there are three types of *waqf*, namely, (i) religious *waqf*, (ii) *waqf* for society and (iii) family *waqf* (Kahf, 2000). From the religious purpose *waqf*, there are few types of *waqf* have been introduced and expanded. In managing *waqf* assets, the *Nazir* cannot violate the *Shariah* rule (in order to discharge accountability to Allah). In the same time, he should show his accountability in fulfilling *waqf* objectives addressed by the *waqif*. In order to discharge their accountability, a good governance framework must be in practice in order to guide them reaching their goals

Waqf is a connection between the wealthy and needy. It can also be collaboration within the society in the environment where everybody (with the same status) aims to contribute to each other even though everybody already able to fulfil their needs and wants. *Waqf* from socio economic aspects can be used as a mechanism to increase standard of living within the *ummah*, reduce poverty and difficulties among the poor and maintaining the good living. This is done through fair wealth distribution among the society (Salarzahi et. al 2010). It can be many types of *waqf*, not limited to religious activities only. The forms of *waqf* are depending on types of assets and purpose of the contribution intended by the contributors. *Waqf* is not limited for religious purpose, but is extended to include several aspects of contributions such as education (school and universities), research, health, housing, orphanage, and centers for unfortunate people etc. This unique characteristic differentiates *waqf* from other philanthropic activities as it can directly fulfil the objectives of the contributors. Looking at the nature of *waqf* institution, it can be either classified as a NPO and social enterprise, consistent with the argument of Adnan (2005). It can be further categorized as an Islamic financial institution based on its decision making process.

2.2 ACCOUNTABILITY FROM ISLAMIC PERSPECTIVES

Accountability concept has expanded beyond the basic definition of being called to account for one's actions. It is frequently described as an account giving relationship between individuals. For example, X accountable to Y when



X is obliged to inform Y about X's actions and decisions, in order to justify them and to be responsible for any misconduct. As in *waqf*, *mutawalli* or *nazir* is accountable for the management of *waqf* that has been given to him by the *waqif*. Thus, they are responsible in managing the *waqf* to ensure that the benefit from the fund is given back to society.

Accountability is undeniably a core value of a public management as it holds a promise a fair and democratic governance. Unfortunately, many scholars and practitioners claimed that the dissimilarity of accounting practices is due to the absence of accounting standards and code of corporate governance for *waqf*. Ihsan (2007) suggested that the development of accounting standards and code of corporate governance for *waqf* because it could improve the accountability of *mutawalli* in managing *waqf*.

Ibn Umar A.S. says: "Every one of you is a guardian and is held accountable for that which he is entrusted. A rule is a guardian and is held accountable for that which in his care. A man is a guardian in respect of his household, a woman is a guardian in respect of her husband's house and his children. Therefore each one of you is a guardian accountable for whatever is in your care" (Hadith Bukhari and Muslim). The practice of accountability is highly encourage since the age of Prophet Muhammad S.A.W. Along with the revival of *waqf* institutions has been emerging. The new and modern *waqf* management has out greater emphasize on the principles of accountability (Mikailu & Maishanu) and transparency.

However, the understanding of accountability may differ to each *mutawalli* due to the different nature of *waqf* to the conventional charity practices. To add that, if there is no clear consensus about accountability for *waqf* institutions, as the means to deliver it will vary. A study conducted by Ihsan (2007) who explored the major themes that constitutes the basis of accountability for *waqf* so that the types of information that should be provided by *mutawalli* to various stakeholders are clearly defined.

Therefore, construction of accountability in *waqf* institutions is much needed especially to ensure the *mutawalli*'s accountability. Since *waqf* is charitable, non-profit in nature and a religious entity, the governance process is crucial which is subject to the definition of accountability. Shahul (2000) indicated that Islamic accountability is appropriate for *waqf* due to the religious motive of *waqf* and for *maslahah ummah* (public interest). He suggested that the accountability of *mutawalli* is to be dual in nature; man's accountability to God as Allah's *khalifah* (vicegerent) and man's accountability to men (society). Hence, all human being are being accountable for all resources entrusted to them as well as fulfilling any contract made between them.

2.3 GOVERNANCE AND ACCOUNTABILITY

Governance can be defined as "system and process that ensure that the overall direction, effectiveness, supervision and accountability in an organization" (Cornforth, 2002). The mechanism of governance may comprise governing boards, monitoring systems and signaling mechanism like reporting. The inter-relationship between the governance elements for a good governance framework is shown in figure 1.0. Given the nature of *waqf* institution, it can be classified as a non-profit organization, and social enterprise.

Governance is a very general concept that can refer to all manner of organizations. This means that governance is often defined more narrowly to refer a particular level of governance associated with a type of organization (including public governance, global governance, non-profit governance, corporate governance and project governance), a particular field of governance associated with a type of activity or outcome (including regulatory governance, participatory governance, multilevel governance, metagovernance, and collaborative governance). Governance can be used not only to describe these diverse topics but also to define normative or practical agendas for them. Normative concepts of fair governance or good governance are common among public, voluntary and private sector organizations.

Grindle's (2004) notion of good enough governance has a significant influence on the development thinking of the institutions of global governance. It refers to accepting a more nuanced understanding of the evolution of institutions and governments capabilities and being explicit about trade-offs and priorities in a world in which all good things cannot be pursued at once.

Accountability in governance is basically holding public officials responsible for their actions. It is concerned with the need to ensure that public funds are spent for the purposes specified and without personal gain to any private individual beyond fair compensation for his or her services. Accountability is imperative to make public officials answerable for government behavior and responsive to entity from which they derive their authority while consciously aware of accountability before Allah in the hereafter.

Figure 1: Model of Good Governance Framework



Source: <http://www.governingtogether.ca>

As part of good governance and best practices of *waqf* institutions' accounting is believed to be able to improve the accountability and transparency of *nazir*. Besides, accounting is means of discharging their accountability to many parties such as *waqif*, *waqf* board, government and community. However, *waqf* institutions could depends solely on accounting to discharge their accountability. A solid governance process and structure by the board and management could also enhance the accountability of *waqf* institutions. As *Waqf* institutions can also be categorized as a non-profit organization, it is useful to adopt set of principles to guide their decision making activities as well as the behavior of the employees, volunteers, and board members. Within an organization, the principles and practices of ethical accountability aim to improve both the internal standard of individual and group



conduct as well as external factors. Based on charity context, Cordery and Morley (2005) proposed the charity accountability as they assume that this sector has specific characteristic compared with business entity. In line with this, Cutt and Murray (2000) agree that accountability framework in non-profit organizations should be define as these institutions have a broad range of constituencies. *Waqf* is not only charitable and non-profit in nature, but also located in religious setting. Therefore, a unique governance process might be implement in the institutions.

In the context of Islamic Financial Institutions (IFIs), its governance is at the stage of infancy with most of the measures performed internally at the initiative of the management or the industry regulated by the means of guidelines. In fact, *Shariah* compliance reporting at the moment is not corroborated by the external independent parties. For that matter, investors and regulators know little how IFIs management exercises the measures to comply with the *Shariah*. *Shariah* Governance (GC) situated within the domain of corporate governance, which is broadly defined as a set of processes, policies and law that could affect organization's way in being directed, administered and controlled. On top of ensuring a proper framework established in the corporation, IFIs also has the responsibility in ensuring that their operations comply with the *Shariah* principles, including in their products, practices, management and etc. Comprehensive compliance with *shariah* principles would boost confidence to the general public and financial markets on the credibility of IFIs operation. In addition, non-compliance towards *shariah* aspects would expose the IFIs to risks, such as reputational risks and fiduciary risk.

The Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI) is an Islamic international autonomous non-profit corporate body that prepares accounting, auditing, governance, ethics and *Shariah* standards for IFIs and the industry. Its standards are followed as part of regulatory requirement if IFIs internal guidelines. In jurisdictions that offer Islamic finance across Middle East, Asia Pacific, South Asia, Central Asia, Africa, Europe and North America. AAOIFI standards have introduced greater harmonization of Islamic finance practices across the globe. AAOIFI outlines seven principles for governance standards, namely *Shariah* Supervisory Board, *Shariah* Review, Internal *Shariah* Review, Audit and Governance Committee, Independence of *Shariah* Supervisory Board, Statement of Governance Principles and Disclosure for IFIs and Corporate Social Responsibility Conduct and Disclosure. Thus, the difference from governance of conventional and IFIs can be summarized as Table 1.

Table 1. Governance: Conventional VS Islamic Financial Institution

Function	Conventional financial institution	Addition in Islamic financial institution
Governance	Board of Directors	<i>Shariah</i> Board
Control	Internal auditor External Auditor	Internal <i>Shariah</i> Review Audit External <i>Shariah</i> Review
compliance	Regulating & Financial Compliance Officers, unit/department	Internal <i>Shariah</i> Compliance Unit

Governance is focusing on the agenda in all sectors – public, private and voluntary. As the voluntary organizations' main objective is to serve for public benefit, they are expected to demonstrate how well they are governed. Good governance is a vital part of how voluntary and community organizations operate and are held accountable. Other sectors have developed codes over the past decade. For example, the public sector has introduced the Good Governance Standard for Public Services in 2004 and the private sector has its UK Corporate Governance Code which is continues to be developed in light of recent governance failures.



The original Good Governance: a Code for the Voluntary and Community sector in the UK arose from directly expressed needs in the sector. These needs was addressed from organizations which wanted guidance to clarify the main principle of governance and to help them in decision making, accountability and the work of their boards. Because of the demand, a group of voluntary sector infrastructure associations, with the Charity Commission came together and decided to work towards developing the Code. Therefore the Code was developed by and for voluntary and community organizations. There six principles that are designed to be universal and applicable to all voluntary and community organization. It is the practice and procedures which will vary according to the type and size of the organization. The six principles are follows: 1) an effective board will provide good governance and leadership by understanding their role, 2) an effective board will provide good governance and leadership by ensuring delivery of organizational purpose, 3) an effective board will provide good governance and leadership by working effectively both as individual and as a team, 4) an effective board will provide good governance and leadership by exercising effective control, 5) an effective board will provide good governance and leadership by behaving with integrity and 6) an effective board will provide good governance and leadership by being open and accountable.

3. RESEARCH OBJECTIVES AND DESIGN

This study is aimed to examine the governance process in Indonesian *waqf* institutions. Abdul Rahman et al. (1999) stated that good governance is needed for the improvement of *waqf* management. The study, hence, proposed for a study that focus on the structure and management of *waqf* administration. Ihsan (2007) focused on *waqf* accounting in Indonesia *waqf* institutions, however ignoring good governance process towards enhancing the accountability in the institutions. Therefore, this study will focus on good governance by answering these research questions:

1. How are governance process are being conducted in Indonesia *waqf* institutions?
2. Does shariah governance exist in the institutions?

This study investigates two sites to answers the above questions, namely Institution 1 and Institution 2. The research choose these two institutions to be consistent with the study of Ihsan and Ibrahim (2011). The data were collected through interviews from persons who in charge of the management of the institutions and also a director. The interviews focused on the governance of the two *waqf* institutions and last around one hour. To ensure that every statement is recorded, the research interviews were taped. The interviews was held on January 26 until January 29 2014 in selected *waqf* institutions in Indonesia.

4. PROFILE OF THE SELECTED WAQF INSTITUTIONS

The first selected institution is Institution 1. Institution 1 was formed by the Yayasan Pesantren Islam (YPI) to develop and manage *waqf* in support of education and *dakwah*. The formation of this body was inspired by the model of *waqf* management in Al Azhar, Egypt. The purpose of the institution id to alleviate poverty in Indonesia besides its vision and mission to return the assets owned by the mortgaged Indonesia. The main *waqf* contributor (*waqif*) of the institution is individuals. Most of them are colleagues of the director of the institution itself. There are no fixed *waqif* in Institution 1 since most of them are individuals who willingly donate *waqf*. To maintain its relationship with the *waqif*, Institution 1 regularly held a joint open fasting with the management company.

Institution 2 is the second institution that was chosen for the study. It was founded in 2004 as described by the Constitution number 41 of 2004. The purpose of the establishment of the institution is to promote and develop the



waqf in Indonesia in order to manage them professionally that will benefit the *ummah*. Before the law was imposed, *waqf* in Indonesia were managed poorly in a traditional way as they are no specific rules and guidelines emphasizing the management of *waqf*. In regards of the new law, *waqf* are now managed productively by *waqf* institutions to bring forward the national *waqf*. Institution 2 is an independent body that is responsible towards building the Islamic economy in the country.

5. FINDINGS AND DISCUSSIONS

The findings from Institution 1 and Institution 2 provide some insight of how *waqf* are governed and how far the good governance are practiced in Indonesia *waqf* institutions. As discussed in prior literature, governance is process that could ensure that the overall direction, effectiveness, supervision and accountability in an organization (Cornforth, 2002). One of principles of good governance is the governing boards. The board composition, education background and leadership style could ensure that accountability have being discharge in an institution.

The board of Institution 1 is chaired by a Director and Chief Executive Officer. The appointment of Chief Executive Officer are made on trust basis. The selection is done by the board members based on the board members' perception on whom they believe will be able to lead the organization. Appointment and such recommendations to the main board are made by observing their character and leadership of the persons. Given this scenario, the appointment of the Chief Executive Officer is weakly managed as they only select on trust basis though an element of Islamic CG can be seen through the implementation of *Shura* (Means consultation where a group of people votes to elect a leader through a binding decision making process). If these appointment is taken more seriously, a more capable leader could be selected to manage Institution 1. In the future, Institution 1 aims to include the involvement of the institutions members in the appointment of the main board. If the appointed boards does not meet the criteria as a leader, poor management is expected to occur in the future that will also indirectly affect the *waqf* governance in the institution.

Institution 2 consists of Executive Agency and the Advisory Council, each led by a Chairman and two Vice Chairman that will be elected by the members. The number of Institution 2 members are made up of at least twenty persons and a maximum of 30 people from elements of society. The members of Institution 2 are appointed and dismissed by the President of Indonesia. The members are appointed for a term of three years and may be appointed for another one term. Institution 2 has five divisions, *Nazir* coaching, managing *waqf*, public relation and research and development. It cannot be determined who is the regular *waqf* donor at Institution 2. However, *waqif* is able to donate to Institution 2 by visiting the partner bank of BWI as they are provide the service as *Nazir* where the public can donate to the *waqf* through their bank. These contribution will be collected and transferred to Institution 2. In Institution 2 there is no special bond to maintain the relationship between the *Nazir* and the institution itself.

In developed economies, auditing is deemed significant because the process of wealth creation and political stability depend heavily upon confidence in processes of accountability, and how well the expected roles are being fulfilled (Sikka et al, 1998). As such, the courts, regulatory agencies and various stakeholder groups have played their parts in demanding that the profession move in an expeditious fashion to meet its responsibilities as perceived by the public.

For every financial year end, Institution 1 will be audited by an appointed external auditor to show their responsibility in managing the *waqf* fund. Unfortunately, there is no internal audit as they believe it is not required given that their directors are competent enough to manage the institution expertly. Annual budget is prepared relating to distribution and funding *waqf* fund every month. For approval of financing decision, the management



must obtain approval from the Director of Finance if the cost is between 1 million Rupiah to 50 million Rupiah. If the amount is above 50 million Rupiah until 100 million Rupiah, they must obtain permission from the Chief Executive Officer.

Similarly, every financial year, Institution 2 is audited by external auditor and government auditor as a means of responsibility for transparency in managing the fund. Institution 2 does not have an internal auditor because the directors are capable and competent in the field of *Shariah* and Islamic Economic. Issues in the spending costs associated with the operations, management must obtain prior approval to the Executive Director. In connection with the program that is already running and to verify whether the program is running well or not, the directors always held a meeting a few times a month. Relating to financial supervision, Institution 2 prepares monthly budget reports on the funding and distribution of the *waqf* funds.

Looking at the corporate governance practice, each institutions are audited by external auditor annually but they do not have their own auditor for internal auditing purposes which proves a poor governance is in place. Not only external auditing is crucial but internal auditing in desperately needed to ensure a better governance. Though they believe that their board is able to monitor the business, it is highly recommended to hire an internal auditor which specialize in auditing to ensure segregation of duties among each employees not forgetting the employer as well. It is known that segregation of duties will prevent conflicting issues in performing their task as only expert know their job well compared to others.

It can be observed, however, that Institution 1 and Institution 2 has a sound internal control in term of usage of money. Both institutions need to gain approval from the board before proceeds with its spending. Boards are being accountable for the decision in these governance process. Budgets are also used by the institutions as a control mean when it comes to funding and distribution of the *waqf* funds.

As Islamic institutions that handle assets, a sound *Shariah* governance is needed in the institutions to ensure that accountability can be effectively discharged. Institution 1 and Institution 2 have their own *Shariah* board/committee. In Institution 1, *Shariah* board consists of members with doctoral background in both religious and social sphere field. To prevent any deviation in their business against the *Shariah*, the *Shariah* council always consult with Majelis Ulama Indonesia as they are a government agency to refer any fatwa related matters. In the case of *waqf*, the board of directors will refer to the *Shariah* board entering any financial decisions to make sure that it does not prohibited in *Shariah* law.

Instead of *Shariah* board, Institution 2 has a *Shariah* Committee that consists of five members from different educational background. There are committee members with doctoral educational background which are expert in Arabic literature, religion, Islamic Economics and business administration. However, there is no specific *Shariah* Board because all the members are *Shariah* experts.

It can observed that these institutions are govern by *shariah* governance as they believe that it is vital practice for Islamic institutions. They have their own *shariah* board that comprises of different educational background to cater the organizational needs. A current study had identify the issues and challenges in *shariah* governance that relates to *shariah* audit (Abdul Rahim, 2008). He argued that *Shariah* audit is needed to complement the current governance mechanism of the Islamic financial service industry. Thus, it can be concluded that *shariah* audit is indeed important in Islamic institutions that managed assets. However, as discussed earlier, both institutions do not engage in internal audit exercise. On top of that, there are no *shariah* audit procedure perform on the institutions to ensure accountability are being discharged.



6. CONCLUSION

Waqf is an important philanthropic institution where it can be utilized to increase the socio-economic of *ummah*. The accountability of the *waqf* management and the involved parties is very high due to the source of *waqf* capital that come from public. The donors put their trust (*amanah*) to management of the institutions and expect their contribution will be managed accordingly to donors' intention. Within this environment, the topic of *waqf* institution governance comes to the picture. This paper examines and compares the governance practices of the two recognized *waqf* institutions in Indonesia. The findings show that there are some degree of differences in the selected governance aspects of the existing structure and practices, such as related to the appointment process of the CEO and higher management and their background of education. In addition, there is no sufficient monitoring mechanism exists in terms of *Shariah* audit in both of institutions, while it is considered as a vital components in Islamic financial institutions worldwide. As such, there are lots of initiatives should be taken especially by the government for this purpose. Future studies should be done on comparison of the *waqf* institutions in Malaysia and Indonesia related to the internal governance mechanism to enhance the management accountability.

References

- Abdul Rahim. (2008). Shari'a Audit for Islamic Financial Services: The Needs and Challenges. *ISRA Islamic Finance Seminar*. Kuala Lumpur.
- Abdul Rahman , A., Bakar, M., & Ismail, Y. (1999). *Current Practices and Administration of Waqf in Malaysia: A Preliminary Study, Unpublished Awqaf Report*. Malaysia.
- Adnan, M. (2005). Akuntansi dan Auditing Kelembagaan Wakaf [Accounting and Auditing for Waqf Institutions]. *Akuntansi Syariah, Arah, Prospek & Tandangannya* (pp. 143-152). Yogyakarta: UII Press.
- Budiman, M., & Wiranata Kusuma, D. (2011). The Economic Significance of Waqf: A Macro Perspective. *The 8th International Conference On Tawhidi Methodology Applied to Islamic Microenterprise Development*. Jakarta.
- Cajee, Z. (2008). The Revival Of Waqf In Muslim Communities: Implementation Of The Recommendations Of The International Waqf Conference South Africa, Cape Town, 2007 . *International Conference on Waqf and Islamic Civilization*. Cape Town, South Africa.
- Conforth, C. (2002). Making Sense of Co-operative Governance: Competing Models and Tensions . *Review of International Co-operation* , Vol. 95 Issue 1, 51-57.
- Cordery, C., & Morley, R. (2005). Hegemony, Stakeholder Saliance and the Construction of Accountability in the Charity Sector. *AFAANZ Conference*. Melbourne.
- Dahlia Ibrahim, & Hasnidar Ibrahim. (2013). The Revitalization of Islamic Trust Institution Through Corporate Waqf . *4th International Conference on Business and Economic Research Proceedings*. Bandung.
- Febryansyah, M., & Amiruddin, M. M. (2014). *Accountability Reports Endowments Research Institute in Indonesia: Badan Wakaf Indonesia, Wakaf Al Azhar and Tabung Wakaf Indonesia*.



- Hassan, A., & Shahid, M. (2010). Management and Development of the Awqaf Asset. *The Tawhidi Epistemology: Zakat and Waqf Economy* (pp. 310-325). Selangor: Jurnal Hadhari.
- Hilal, F. N., Febryansyah, M., Amiruddin, M. M., & Mansour, I. Q. (2013). Management of Waqf, Study Case In Waqf Institution in Indonesia: Wakaf Al Azhar and Tabungan Wakaf Indonesia.
- Hisham, Y. (2006). *Waqf Accounting in Malaysias State Islamic Religious Institutions: The Case of Federal Territory SIRC*.
- Ihsan, H. (2007). Towards the Improvement of Waqf Accountability in Indonesia: A Critical Review of the Act No 41/2004 on Waqf. *Jurnal Akuntansi & Manajemen Vol 2 No.2*, 71-80.
- Ihsan, H. (2007). WAQF Accounting and management in Indonesian WAQF institution. *the cases of two WAQF foundations*.
- Ihsan, H., & Adnan, M. (2009). Waqf Accounting and the Construction of Accountability. *International Conference in Waqf Laws and Management*. Gombak.
- Ihsan, H., Ayedh, A., & Shahul, H. M. (2006). Towards The Betterment Management and Transparency of Waqf Institutions: Lesson Learned from the Charity Commission. (pp. 27-46). Al Risalah.
- Junaidi, A. (2014, January 26-29). Accountability Reports Endowments Research Institute in Indonesia: Badan Wakaf Indonesia, Wakaf Al Azhar and Tabung Wakaf Indonesia. (M. Febryansyah, & M. Amiruddin, Interviewers)
- Kahf, M. (2003). The Role of Waqf in Improving The Ummah Welfare. *International Seminar on Waqf as a Private Legal Body*. Indonesia.
- Lewis, M. K. (2001). Islam and Accounting. *Accounting Forum* (pp. 104-127). Blackwell Publishers Ltd.
- Masruki, R., & Shafii, Z. (2013). The Development of Waqf Accounting in Enhancing Accountability. *Middle East Journal of Scientific Research*, 1-6.
- Mikailu, A., & Maishanu, M. (n.d.). Islamic Value System, Accountability and Transparency in The Public Service.
- Mohamed Isa, Z., Ali, N., & Harun, R. (2011). A Comparative Study of Waqf Management in Malaysia. *International Conference on Sociality and Economics Development* (pp. 561-564). Singapore: IACSIT Press.
- Murray, V., & Cutt, J. (2000). Accountability and Effectiveness Evaluation in Non-profit Organizations.
- Ramli, N. M., & Muhamed, N. A. (2013). Good Governance Framework for Corporate Waqf: Towards Accountabilty Enhancement. *Proceedings Of World Universities' Islamic Philanthropy Conference 2013*. Kuala Lumpur.
- Salarzahi H, Amesh H, & Nibkin D. (2010). Waqf as a Social Enterpreneurship Model In Islam. *International Journal of Business and Management Vol. 5 No. 7*.
- Shafii, Z., & Salleh, S. (2010). Enhancing Governance, Accountabilty and Transparency in Islamic Financial Institution: An Examination Into The Audit of Shari'a Internal Control System. In *Malaysian Accounting Review, Special Issue Vol. 9 No. 2* (pp. 23-42).



- Shahul, H. (2000). The Need For Islamic Accounting: Perception of Its Objective and Characteristics by Malaysian Accountants and Academics. Unpublished PhD Thesis.
- Sikka, P., Puxty, A., Willmott, H., & Cooper, C. (1998). The Impossibility of Eliminating the Expectation Gap: Some Theory and Evidence. *Critical Perspectives on Accounting*, 299-330.
- Sirojudin, S. (2004). Toward Welfare Pluralism: Policy and Practice of the Islamic Welfare Effort in Indonesia.
- Tunku Alina Alias. (2012). Venture Capita Strategies in Waqf Invesntment and Spending. *ISRA International Journal of Islamic Finance*, 99-126.
- Willems, T., & Van Dooren, W. (2012). ombining Multiple Forums and Functions. *Coming To Terms With Accountability*, 1011-1036.
- Yunanda, R. A., & Abd. Majid, N. (2011). The Contribution of Islamic Ethics Towards Ethical Accounting Practices. *Issues In Social and Environmental Accounting*, pp. 123-137.

Faculty of Economics and Muamalat
Universiti Sains Islam Malaysia (USIM),
71800 Bandar Baru Nilai, Negeri Sembilan,
MALAYSIA



OWNERSHIP STRUCTURE AND RISK TAKING OF MALAYSIAN BANKING INSTITUTIONS

NASYRA AB. JAMIL, RASIDAH MOHD SAID, FAUZIAS MAT NOR

UKM-Graduate School of Business,

Universiti Kebangsaan Malaysia,

UKM-Graduate School of Business, Universiti Kebangsaan Malaysia, 43600 UKM Bangi, Selangor,
MALAYSIA.

nasyee_3180@yahoo.com, rasidah@ukm.edu.my, fauzias@ukm.edu.my

ABSTRACT

This study aim to provide the impact of ownership structure on bank risk takings by using Z-Score based on the formulation that fits the context of Malaysia as the emerging country. Besides, this research also investigates the impact of ownership structure on Z-Score with capital adequacy ratio as the moderating factor along with the other variables. By using secondary data, the analysis of this study is narrowed to the eight Large Domestically-owned Commercial Banks in Malaysia of period 2000-2012. The results suggest that there are mix findings of the relationship between the ownership structures towards Z-Score. In addition, the result also showed that there are also significant findings of capital adequacy as the moderating factor which contribute the objectives of the research in investigating the effect of ownership structure on Z-Score with capital adequacy ratio as the moderator. However, likewise, the finding shows that the direct effect of capital adequacy ratio towards Z-Score is found not to be significant. The indications of the regression results towards the eight Large Domestically-owned Commercial Banks in Malaysia also are discussed accordingly.

Keywords: Ownership structure, risk taking, banking, Z-Score, capital adequacy ratio



1. INTRODUCTION

Two clear messages from the corporate governance literature show that ownership is important and that it is helpful to view the issue in the context of the principal-agent framework and public choice theory (Altunbas et al. 2001). However, while that literature has provided considerable understanding of the effects of ownership, its primary focus is basically on non-financial firms. The separation of owners (financial provider) from decision maker (manager) creates agency problem between these two entities in the firm. Agency problem arises when shareholders yearn for capital return while the decision maker may misappropriate the shareholders' investment. Agency problem is a source of inefficiency because it explains why environmental pressures, which influence the responses and effort of management, may fail to coerce maximal effort from managers.

According to Levine (2004), principal-agent problems in banks may raise the issues attributable to what is the most appropriate governance structure for banks. The complicated issues of bank governance is caused by several factors such as the quality of bank regulations and supervision, the opaqueness of bank assets, the level of market development, and the institutional environment which conditions the overall effectiveness of financial markets. Iannotta et al (2007) argues that a firm's ownership structure can be defined along two main dimensions. First, the degree of ownership concentration; firms may differ because their ownership is more or less dispersed. Next, the nature of the owners; given the same degree of concentration, two firms may differ if the government holds a majority stake in one of them, which is similarly a stock firm with dispersed ownership is different from a mutual firm.

Bank stability has been yet again the topmost agenda for the policy makers' agenda across advanced developing countries. This has been a concern since the beginning of the 1997-1998 Asian financial crisis, and for the past few years there has been numerous debates around the world on to the stability of banks of different sizes and ownership (Beck et al 2009). For the past two decades, Malaysia has experienced two financial crisis namely; Asian Financial Crisis in 1997-1998 and the Global Financial Crisis in 2008-2009. The 1997/1998 Asian Financial Crisis has been found to be more severe and have left a bigger impact to Malaysia banking industry as compared to the 2008-2009 Global Financial Crisis. As per Beck et al. (2003) the occurrence of the banking crisis is due to the banking fragility, whereby crises are less likely in economies with more concentrated banking systems. This is because the profits enhanced by the concentrated banking systems do resulted lower bank fragility. The same issue also has been discussed in (Beck et. al 2006).

The aim of this research is to investigate the ownership structure as a mechanism for analysing the determinants of Malaysian bank risk taking. The main motivating factor of this study is the effect of the 1997/1998 economic crisis. In addition, prior to the situation, the poor bank governance are more severe than that of non-bank firms and their failures have even more significant costs. This is due to banks are considered unique economic units because their distinguishing roles in financial intermediation, in payment system, liquidity, information and maturity and denomination transformation. In line to this, banks are also important as they provide critical monitoring role in the governance of their borrowers such as reducing borrowers' earnings management behaviour as suggested by Ahn & Choi (2009).



Pathan (2009) points the importance of studying bank risk-taking today is far more important than ever before due to the constant attempt of legislation revision. All the attempts by the policy makers is to facilitate a better monitoring of the bank activities which includes the bank risk taking behaviour. Besides, the financial shocks in the US such as the sub-prime mortgage crisis in August 2007 due to the irresponsible risk-taking by the financial institutions, do initiate the economy at risk. As the result, it is crucial to study on bank risk taking.

Even though there is an increasing number of study and research on bank risk taking, it is found that most of the studies were done on developed countries and very few studies done on developing countries. There is a need of the bank risk taking studies in developing countries such as Malaysia because there is a concern whether or not the approaches and results of the studies conducted in developed countries could be generalized and whether it is applicable to the developing countries context such as Malaysia.

Bank risk taking is measured by Z-Score that is commonly employed as risk measure in empirical banking literature. This measure reflects the probability of insolvency of the sample banks. In addition, this study also attempts to investigate the importance of capital adequacy ratio (CAR) as a moderating factor between the ownership structures with the bank risk takings. Capital adequacy ratio (CAR) is the ratio of a bank's capital to its risk.

The first proposed problem statement for this research is as such:

1. Does the bank ownership structure affect the bank risk taking in Malaysia?

Since capital adequacy ratio (CAR) is the moderating variable used in this research, the second research problem is as below:

2. Is there any impact on ownership structure with bank risk taking with capital adequacy ratio as the moderating factor?

Based on the former research problem statement, with the research objectives are as follows:

- i. To investigate the effect of ownership structure and bank risk taking.
- ii. To investigate the interaction of CAR on ownership structure with bank risk taking.

The importance of conducting this research are as such:



Firstly, most of the previous studies have not investigated on how ownership structures interact in shaping the risk taking of banks (Laeven & Levine 2009). This study will focus on the effect of the five types of ownership structure (bank, financial company, industrial company, mutual fund and government) towards bank risk takings. In addition, this study will also investigate the interaction effect of capital adequacy ratio as the moderating variable.

Secondly, standard agency theories suggest that ownership structure influences corporate risk taking (Jensen & Meckling 1976 ; John et al. 2008). Although, this issue is important and crucial in creating awareness among corporate policy makers, literature and discussion, however, are still lacking. Hence, there is a need to study the influence of ownership structure towards risk taking and in this research context will be the bank risk taking. This gap is believed to have a serious potential from a policy maker perspective.

Finally, this study will also add in the body of bank literature since there is the need and not much of bank risk taking study in developing countries. Most of the studies and measurement on bank risk takings focused to the developed countries (Rahman et al. 2012). This study also contributes to the measurement of bank risk taking behaviour that is applicable to the developing countries such as Malaysia.

This paper is organized as follow. Section 2 discusses the literature related to agency theory with special emphasis on bank risk taking. The hypotheses of this research are developed at the end of the section. Section 3 discusses the methodology and the data employed in this study. Section 4 presents and discusses the results of this study. Finally, Section 5 concludes the main findings of the study.

2. LITERATURE REVIEW

The diversified range of Malaysian financial institutions is merely to serve the various and yet complex needs of the domestic economy. The Malaysian financial system consists of the conventional financial system and the Islamic financial system, which co-exist and operates in parallel. In Malaysia, the central bank which is also known as Bank Negara Malaysia which is on the top of the monetary and financial structure of the country.

The banking system is the primary mobiliser of funds and also the main source of financing that supports the economic activities in Malaysia. It comprises of commercial banks, investment banks and Islamic banks. In this study, the focus is on the eight Domestically-owned Commercial Banks in Malaysia. This is due to their importance as the largest group of commercial banks and most significant providers of funds in the banking system. Furthermore, commercial banks have the largest share of the market. The classifications of the eight commercial banks are as provide in Table 1.



Table 1: The classification of the three main group of commercial banks

Family Owned Banks	Government Owned Banks	Corporate Owned Banks
AMMB	Affin	Alliance Bank Berhad
HLB	CIMB	
Public Bank	Maybank	
RHB		

The worsening situation that have been prompted in some of the banking institutions in the early 1998 has initiate the Malaysia government for a sudden decision for a bank merger programme in 1999 in order to consolidate the banking industry as some banking institutions faced difficulties due to their substantial losses and the increase of NPL ratios (Lum & Koh 2007).

A robust bank merger programme was initiated by the government in July 1999 in order to restructure all domestic banking institutions into six banking groups (Lum & Koh 2007). Referring to the Bank Negara Malaysia annual report 2001, there are ten lead anchor banks namely; Affin Bank Group, Alliance Bank Group, Arab Malaysia Bank Group, Bumiputra-Commerce Bank Group, EON Bank Group, Hong Leong Bank Group, Malaysian Banking Group, Public Bank Group, RHB Bank Group and Southern Bank Group. The composition of the ownership structure in the merged banking groups and the market structure of the banking industry usually changes due to the consolidation of the banking industry. The Malaysian government's strategy in the post-crisis years is to consolidate the banking industry (Lum & Koh 2007).

As for the ownership control structure, the domestic banking groups such as Affin Bank Berhad, Bumiputra-Commerce Bank Bhd., EON Bank Berhad and Maybank Bhd. are categorized as government connected ownership. The ownership control structure for Alliance Bank Malaysia Bhd. and Southern Bank Bhd are corporate ownership and widely held. On the other hand, the domestic banking groups which are family and corporate ownership are Ambank (M) Bhd. which formerly known as Arab-Malaysian Bank Bhd., Hong Leong Bank Bhd., Public Bank Bhd. and RHB Bank Bhd.

It is necessary to study the identity of owners and shareholder concentration in a firm, since there is inconclusive studies of ownership structure as per (Chu, 2004). Besides, the locus of ownership structure lies between the specialization of risk bearing, provision of finance and decision making functions of a firm. According to Gursoy and Aydogan (2002), the concept of ownership structure can be defined along two dimension namely; ownership concentration and ownership mix. As for the former which is ownership concentration, that refers to the share of the largest owner and is influenced by absolute risk and monitoring cost. Meanwhile, while the latter ; ownership mix related to the identity of the major shareholder (Pedersen & Thomsen 1999) . On the other hand, as



per Chu (2004) ownership concentration is divided into dispersed, dominant minority and majority controlled firms. Referring to Hansmann (2000), ownership structure is like the hard core of corporate governance, whereby a firm's "owners" is those persons who share two formal rights to control the firm and the right to appropriate the firms' profits, or residual earnings which in theory this could be separated and held by different classes of persons.

The focus of corporate governance for banks is also different which is due to the banking system's as the financial intermediary role (Lum & Koh 2007). Besides, according to Mehran et al. (2011) the governance of banks can be distinguish into two key differences from that of financial firms. Firstly, the banks have many more stakeholders than the nonfinancial firms and secondly, are that the business conducted by banks is opaque and complex and can shift rather quickly.

The proper management of risk is through good corporate governance mechanisms which provide a framework of disclosure that allows the market to discern the risk choices of the banking institutions. It must entail greater transparency and market discipline in order to be effective (Lum & Koh 2007). As for the Malaysian banking sector, the changes in the ownership structure have been as important feature of the evolution. In Malaysia, the bank ownership structure implies a high concentration of shareholding by ownership types. The BAFIA was a clear and robust regulatory response to the crisis of the mid-1980s, which came into force on October 1, 1989.

As per Section 46 of BAFIA 1989, all banks are required to institutionalize their shareholding structure by restricting ownership in a bank by restrictive the limit of equity ownership by individual companies in bank to no more than 20 per cent as per the Banking act of 1973. On the other hand, the equity owned by family-owned company or an individual is restricted up to 10 per cent. However, it does seem to have any significant effect on the composition of ownership structure in the banking industry even though the consolidated programme have resulted in larger and better capitalized domestic banking institutions.

The government connected bank ownership which comprise of Affin, CIMB and Maybank are categorized as dominant majority type. Alliance bank which is under corporate ownership type is also categorized under dominant majority concentration type. As for the family ownership type, AMMB is categorized as the dominant majority concentration. The remaining in the family ownership type such as Public Bank is categorized as dispersed concentration and the remaining two in family ownership type; HLB and RHB are categorized as Majority controlled ownership concentration. Dispersed structure ownership appears to be greater risk taker compared to dominant minority ownership. However, the risk receptive behaviour increases as share concentration increases.

Referring to the theoretical and empirical literature, the nature of the shareholders does influence the different of agency problems and the risk-taking behaviour. The identified issue raised by Jensen and Meckling (1976) is the conflict of interest between managers and shareholders. In line to this, theory indicates that shareholders with a diversified portfolio are motivated to take more risk for a higher expected return whereas managers take less risk to protect their position and personal benefits and to preserve their acquired human capital Galai and Masulis (1976), Jensen and Meckling (1976), Demsetz and Lehn (1985), Esty (1998).



Garcia-Marco and Robles-Fernandez (2008), revealed there are numerous attempts to quantify and explaining the risk-taking behaviour of financial intermediaries which have been reviewed by the financial literature. In addition to this, the control of the risk-taking in banking do relate directly to the protection of both the depositors and the financial system as a whole. Currently the issue of this topic have been the central in economics and finance. The agency problems and risk-taking behaviour are different according to the nature of the shareholder which has been stressed in the theoretical and empirical literature by Barry, Lepetit, and Tarazi (2009). Jensen and Meckling (1976) identify the first issue which is the conflict of interest between managers and shareholders.

Referring to Galai and Masulis (1976), Esty (1998), Jensen and Meckling (1976), Demsetz and Lehn (1985), the agency theory indicates that shareholders with a diversified portfolio are motivated to take more risk for a higher expected return whereas managers take less risk to protect their position and personal benefit, and preserve their acquired human capital. The first to test empirically and relationship between banks' ownership structure and their risk taking incentives is by (Saunders, Strock, & Travlos, 1990). Moreover, from the findings also reveal that the banks controlled by shareholders tend to take more risk compare to banks controlled by managers. Based on this findings do motivate to undergo for this research.

Based on theory of risk taking predicts that banks with large dominating shareholders, in other words, with easy control over management, tend to take more aggressive risks than managers dominated banks with small disperse shareholdings. Prior studies, in the case of banking found that the existence of large shareholders increases bank risk taking (Ciancanelli and Gonzalez, 2000; Iannotta et al., 2007; John et al., 2008).

The level of risks in banks which refer to bank risk taking, is measured by insolvency risk (Barry et al. 2011). Bank insolvency problem reveal the degree of exposure to losses or failures which will reduce bank capital reserves that could be used to offset adverse shocks. Bank insolvency risk indicates the banks' distance from failure and is measure using Z-Score. A lower (negative) Z-Score indicates a riskier bank, whereas a higher (positive) Z-Score implies a more stable or the bank is safer. The predictions by Saunders et al. (1990) and Laeven and Levine (2006) that banks with large dominating shareholders take larger risks than manager-dominated banks with small shareholdings.

Firstly, based from the findings that bank with different types of ownership structures has different attitudes in term of risk-taking. Besides, the mix findings found by Barry et al. (2009) that there is a negative relationship between the proportion of stock held by families and individuals and asset risk, and there is also a positive relationship between default risk and the proportion of stocks held by institutional investors or non-financial companies. According to Nicolo and Loukoianova (2007), the bank risk is measure by Z-Score which is defined as $Z = (ROA + EQTA) / \sigma(ROA)$ whereby the measure of bank risk is the proxy of banks' profitability of failure. However, the result by Nicolo and Loukoianova (2007) for the bank risk taking is applicable for developed banks.

Empirical studies on the effect of ownership on bank risk takings provide mixed results. Ownership concentration positively affects bank's risk taking (Laeven & Levine 2009). Besides, banks with concentration ownership tend to have better loan quality, lower asset risk and lower insolvency risk (Iannotta et al 2007). Referring



to Laeven and Levine (2009), the ownership stakes to consider consists of ten per cent and twenty per cent with the Z-Score as the bank risks. However, Shehzad, de Haan, and Scholtens (2010) on the other hand, suggest that in order for the result to be different, is by a higher levels of ownership concentration with capital adequacy ratio as the proxies for risk. As the result, the effect of ownership concentration is positive and in a better risk-weighted capitalization with the capital adequacy ratio as the proxy of the bank risk.

The Capital Adequacy refers to a bank's capital or equity whereby it is the margin by which creditors are covered if the bank has to liquidate its assets. Capital to asset ratio, is a good measure of a bank's health, which by law, is required to be above a prescribed minimum.

Both hypotheses formation are as follow:

The relationship between bank ownership and Z-Score

According to Garcia-Marco and Robles-Fernandez (2008) that high concentration ownership in small Commercial bank tends to lead to a greater increase in risk-taking. The situation implicitly is due to higher shareholder concentration that appear linked to a stricter control over managers. This is appearing to be clear evidence for the moral hazard problem which is the increase in risk taking in this kind of institutions. Referring to Laeven and Levine (2009), the diversified owners have stronger incentives to increase risk than non-shareholding managers. As the result, for banks with powerful and yet diversified owners tend to be riskier than widely held banks.

As per Barry et al. (2009), the different ownership structure do imply different levels of risk and profitability. The ownership structure discuss by Barry et al. (2009) consists of government, bank, Financial Company, Mutual and Pension Fund, Nominees, Trust or Trustees, Insurance Company, Individuals and Families. In addition, according to Barry et al. (2009), banks with different ownership structures tends to have different attitude toward risk taking behaviour. This situation is subject to the different ownership structure in the bank, the levels of the risk taking behaviour are varies whether are more or less risky. As per Iannotta et al. (2007), a higher ownership concentration is associated with lower insolvency risk. Thus, this study proposes the ownership structure to be positively associated with Z-Score.

H1 : There is positive relationship between ownership structure and Z-Score

The impact of ownership structure on Z-Score with CAR

According to Naceur and Kandil (2009), since the response of choice by a non-risk averse will be towards a riskier asset, the distribution of risk aversion across banks is due to the effect of capital requirements on the overall



banking system. The potency of more capital at risk through capital requirement enables to internalize the efficiency of investing in high risk assets. In addition, the situation will also reduce the capitalized value of expected future profits which is referring to the reduction of the banks' franchise values.

According to Naceur and Kandil (2009), the banks' capital ratio decisions are significantly affected by the capital requirements. Besides, the regulatory pressure did positively affect their chosen risk levels, although did not induce banks to increase their capital requirement. As per Shehzad et al. (2010), the capital adequacy ratio positively affected by ownership concentration, and as the result ownership concentration reduces the bank riskiness and this can be measure by Z-Score. On the other hand, referring to Dolde and Knopf (2006), ownership structure is associated with higher risk is also associated with higher returns.

The argument raised by Ciancanelli and Reyes-Gonzalez (2000) that capital requirements avoid expropriation problems between shareholders and bank creditors. Referring to La Porta, Lopez-De-Silanes, and Shleifer (1999) and Rime (2001), capital requirement reduce incentives for high risk taking in banking as shareholders are forced to absorb a larger part of the losses. In supporting the findings, Konishi and Yasuda (2004) found that the implementation of high capital requirement reduced bank risk. This indicates and suggests a negative significant relationship between high capital requirement and bank risk taking. In addition, this suggests that the implementation of high capital requirement is important in reducing bank risk.

Referring to Laeven and Levine (2009), the ownership stakes to consider consists of ten per cent and twenty per cent with the Z-Score as the bank risks. However, Shehzad et al. (2010) on the other hand, suggest that in order for the result to be different, is by a higher levels of ownership concentration with capital adequacy ratio as the proxies for risk. As the result, the effect of ownership concentration is positive and in a better risk-weighted capitalization with the capital adequacy ratio as the proxy of the bank risk. Based on prior studies, the current study predicts positive moderation association by capital adequacy ratio between ownership structure and Z-Score.

H2 : CAR positively intervene the relationship between ownership structure and Z-Score.

3. METHODOLOGY

The data used in this study consist of annual ownership and financial data for the eight listed commercial banks in Malaysia during the years 2000-2012. The banks included in the sample are AMMB, HLB, Public Bank RHB, Affin, CIMB, Maybank and Alliance Bank. The data have been gathered from annual reports of the banks, Thomson Financial Datastream data services and Bureau Van Dijk Bankscope. The focus of this research is on commercial banks only.

The ownership data are collected from annual reports of the banks and typically includes the top thirty shareholders. The classification of the ownership structure was gathered from Bureau Van Dijk Bankscope. Usable



data for analysis begins from 2000-2012 due to the Bank merger and acquisition process completed by 2001. For this study, since the aim is to focus on the influence of different ownership structure on bank performance and bank risk takings, the changes of the shareholdings within the year has been excluded. The percentage of the shareholders used in this research is solely from the annual reports while omitting the information of changes available provided by Bankscope. Thus, in order to test both of the models in this research; a balanced panel of data is constructed by collecting yearly data from 2000 until 2012 of eight Large Domestically-owned Commercial Banks in Malaysia which consists of 104 observations.

Below are the discussion of the main categories of variables for this research namely indicators of bank risk takings and ownership structure variables. As such, the model has Z-Score as dependent variables and five ownership structure variables namely (public authorities or governments, financial company, bank, industrial companies, and mutual fund or trustees) as independent variables. In addition, bank size and financial leverage are employed as control variables, and Capital Adequacy Ratio (CAR) as the moderating variable.

In this research, in order to meet the context of emerging market and as proposed by Bank Negara Malaysia regarding the more appropriate measurement of Z-Score, the calculation of this variable is based on the measurement as introduced by (Altman, 2005), and it is as presented below:

$$\text{Z-SCORE} = 3.25 + 6.56 (\text{Working Capital} / \text{Total Asset}) + 3.26 (\text{Retained Earnings} / \text{Total Asset}) + 6.72 (\text{Operating Income} / \text{Total Asset}) + 1.05 (\text{Equity} / \text{Total Asset})$$

The findings by Demsetz and Lehn (2005) do agree of the norm of including variable such as firm size as one of the variable in the regression equation. The formula of the firm size in this research is measured by the natural logarithm of the total assets of the banks. As for this research, bank size is represented by the natural logarithm of bank total assets. Following Lee et al. (2008), bank's financial leverage is measured by capital to asset ratio, and leverage value is represented by the ratio of total debt to common equity. Capital adequacy requirements set by central banks are intended to reduce bank insolvency risk. As for this research, Capital Adequacy Ratio value is calculated as the ratio of total capital to risk weighted assets of banks.

The relationship between bank ownership and Z-Score

In Hypothesis 1, the ownership structure is expected to positively affect towards Z-Score. In order to investigate this hypothesis, Equation (1) is used to determine the relationship between ownership structure and Z-Score.

Model 1

$$\text{Z-Score} = \alpha_0 + \beta_1 \text{GOVOWN}_{it} + \beta_2 \text{FINOWN}_{it} + \beta_3 \text{BNKOWN}_{it} + \beta_4 \text{INDOWN}_{it} + \beta_5 \text{MFDOWN}_{it}$$

$$+ \sum_{j=1}^7 \gamma_j DB_j + e_{it} \quad (1)$$

Where, GOVOWN, FINOWN, BNKOWN, INDOWN and MFDOWN are ownership structure variables, Z-Score is the Z-Score formula used in developing countries. DB_j is a bank dummy variable which is equal to 1 if the bank is Affin Bank and 0 otherwise, 1 if the bank is Alliance Bank and 0 otherwise, and so forth. Besides, Maybank is taken as the reference bank which is selected based on its high total asset for the sample period and e_{it} is the error term. This simple model is tested as benchmark for other models in order to find the relative improvement in model's explanation power. The framework for Model 1 is depicted in Figure 1.

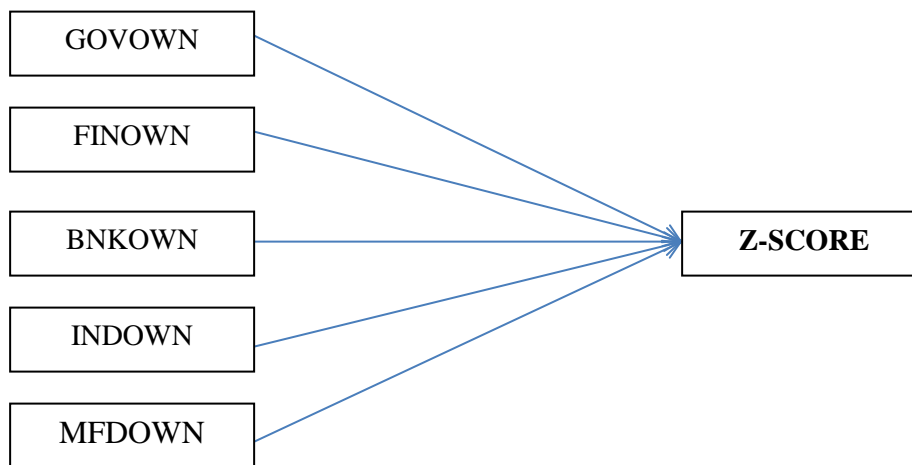


Figure 1: Model 1 framework

Hierarchical moderated multiple regression is used to access the effects of a moderating variable which in this research is the capital adequacy ratio (CAR). Hierarchical moderated multiple regressions, as instance is used since the interaction terms to be enter into the regression equation. As for the hierarchical moderated multiple regression, it is required to enter the main effects, which refers to the five ownership structure variables ; GOVOWN, FINOWN, BNKOWN, INDOWN and MFDOWN on the first step and then the interaction terms in the second step. The framework for Model 2 is depicted in Figure 2.

The impact of ownership structure on Z-Score with CAR

Model 2

$$\begin{aligned} \text{Z-SCORE} = & \alpha_0 + \beta_1 \text{GOVOWN}_{it} + \beta_2 \text{FINOWN}_{it} + \beta_3 \text{BNKOWN}_{it} + \beta_4 \text{INDOWN}_{it} + \beta_5 \text{MFDOWN}_{it} + \\ & \beta_6 \text{CAR}_{it} + \beta_7 \text{GOVOWN} * \text{CAR}_{it} + \beta_8 \text{FINOWN} * \text{CAR}_{it} + \beta_9 \text{BNKOWN} * \text{CAR}_{it} + \beta_{10} \text{INDOWN} * \text{CAR}_{it} \\ & + \beta_{11} \text{MFDOWN} * \text{CAR}_{it} + \beta_{12} \text{LVRG}_{it} + \beta_{13} \text{BNKSZ}_{it} + \sum_{j=1}^7 \gamma_j DB_j + e_{it} \end{aligned} \quad (2)$$



Where, Z-SCORE is Z-Score formula used in developing countries, GOVOWN, FINOWN, BNKOWN, INDOWN and MFDOWN ownership structure variables and (CAR) is the capital adequacy ratio. BNKSZ is the bank size and LVRG is the bank's financial leverage. GOVOWN*CAR, FINOWN*CAR, BNKOWN*CAR, INDOWN*CAR and MFDOWN*CAR are the interaction variables generated by multiplication of capital adequacy ratio and by ownership structure variables. Interaction variables between capital adequacy ratio and ownership structure are generated and added to the model in order to test the moderation effect of capital adequacy ratio as in the regression result in Model 2a in Section 4 later. On the other hand, as in Model 2b regression results is incorporated since capital adequacy ratio besides as the moderation effect, may also have direct effect on Z-Score. DB_j is a bank dummy variable which is equal to 1 if the bank is Affin Bank and 0 otherwise, 1 if the bank is Alliance Bank and 0 otherwise, and so forth. Maybank is taken as the reference bank which is selected based on its high total asset during the whole period of study, and e_{it} is the error term. The framework for Model 2 is depicted in Figure 2. This model assumes that capital adequacy ratio has moderating effect as well as direct effect on the Z-SCORE whereby the direct relationship of CAR and Z-SCORE is represented by the broken lines. The control variables are included, which referred to the bank's size and bank's financial leverage.

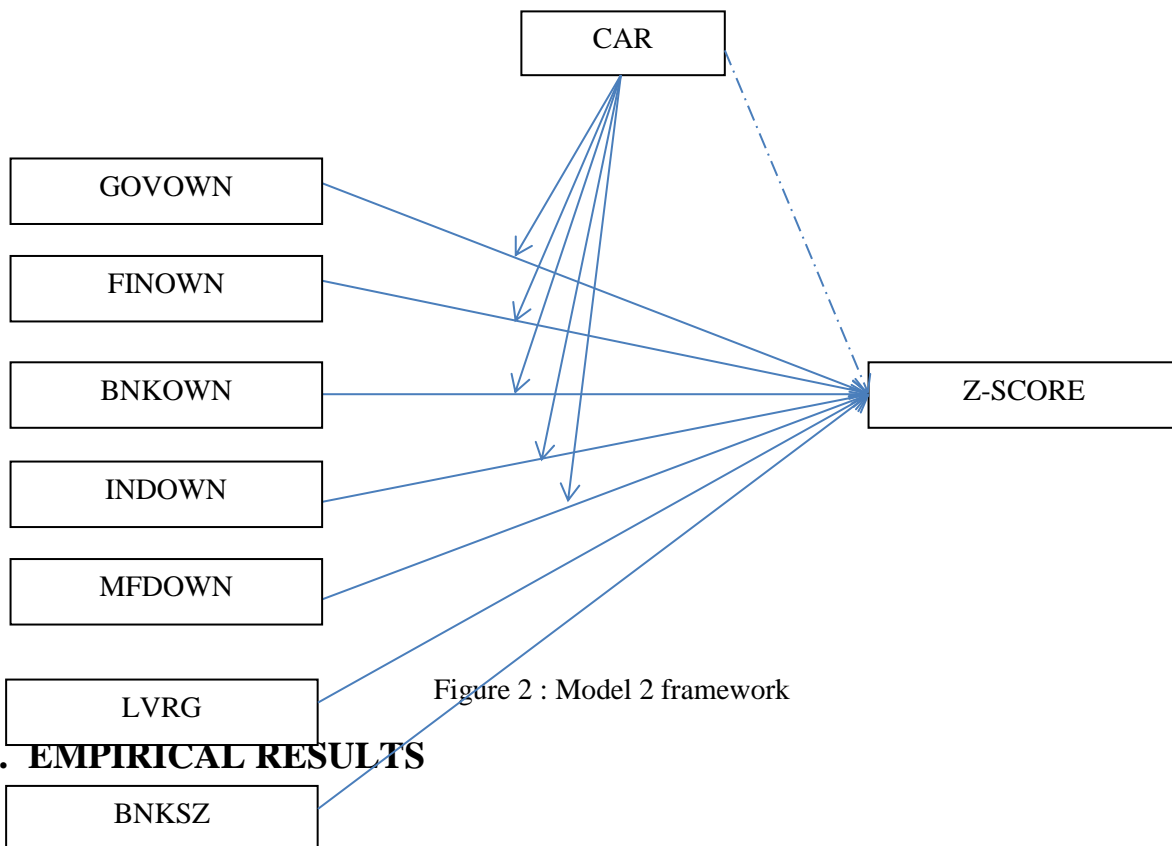


Figure 2 : Model 2 framework

4. EMPIRICAL RESULTS

Summary of the sample descriptive statistics of ownership structure variables, risk measure; Z-Score, moderating variable, and control variables for the overall sample for the eight commercial banks are presented in Table 2. Total number of observations in this study for each variable is 104, which came in the form of a panel data of eight cross sections (i.e. commercial banks) and time series of thirteen years. Panels of data are all balanced with no missing data. From the descriptive statistics results, for government ownership with mean value 18.24 per cent is the second largest ownership structure for the eight commercial banks. The largest ownership type with the mean value 40.3 per cent is MFDOWN which referring to mutual fund ownership structure. On the other hand, INDOWN or



industrial company ownership, on average the shareholdings of the overall banks is 7.28 per cent. BNKOWN and FINOWN ownership structure are considered to have low shareholdings among the five ownership structure with the shareholdings of 3.61 percent and 2.97 per cent, respectively.

Table 2: Descriptive statistics for the variables of the research

	Mean	Median	Maximum	Minimum	Std. Dev.	Observations
GOVOWN	0.182379	0.115100	0.816600	0.000000	0.173771	104
FINOWN	0.029743	0.009200	0.354000	0.000000	0.057918	104
BNKOWN	0.036083	0.000000	0.710500	0.000000	0.102187	104
INDOWN	0.072786	0.002800	0.336400	0.000000	0.099978	104
MFDOWN	0.402992	0.375200	0.839500	0.015600	0.226953	104
ZSCORE	4.103858	4.137023	4.684855	2.679222	0.305935	104
CAR	0.146595	0.144900	0.238000	0.115500	0.020798	104
BNKSZ	18.17131	18.16604	20.01717	13.96907	0.895839	104
LVRG	2.152660	1.747700	8.746700	0.254100	1.505984	104

The mean for the moderating variable is 14.66 per cent, with maximum of 23.8 per cent and minimum of 11.55 per cent which all above the requirement of banking regulation of the capital requirement of 8 per cent. On the other hand, Z-Score with the mean value of 4.10 and maximum of 4.69 indicate that the sample of the banks are stable in term of insolvency risk and are in the range of a safe zone. On the other hand, the minimum Z-Score of 2.68 indicates that the effected banks are in a range of grey zone. None of the banks in the sample in the distress zone Altman (1968). As for the sample commercial banks have the means value of RM18.17 million for the bank size and 2.152660 for the ratio of total debt to total equity which is denoting to the financial leverage.

The relationship between bank ownership and Z-Score

Model 1

Result of the regression analysis conducted on Model 1, Model 2a, Model 2b and Model 2 are presented in Table 3. The F-statistic (4.497761) suggests that the model is statistically significant. It indicates that, as a whole, the model which consists of the five ownership structures does have a significant effect on Z-Score. The coefficient of the ownership structures; GOVOWN (-0.048552), FINOWN (-0.617332) BNKOWN (0.256063), INDOWN (-



0.491610) and MFDOWN (0.245771), which are not significant even at 1 per cent level, have a negative sign for GOVOWN, FINOWN, INDOWN, and positive sign for BNKOWN and MFDOWN. In other words, GOVOWN, FINOWN, INDOWN have a negative relationship with Z-Score and BNKOWN and MFDOWN have a positive relationship with Z-Score.

Besides, the results also show that Maybank, as the reference bank based on its high total asset for the period, has a positive effect and is significant towards Z-Score. The Z-Score for Affin is higher than the Z-Score for Maybank by 0.190376. In addition, the other three banks' Z-Score that are higher than Maybank Z-Score are AMMB, CIMB and PBB with the value of 0.236173, 0.141758 and 0.247088 higher than Maybank's Z-Score. On the other hand, Alliance, HLB and RHB do have lower Z-Score than Maybank by 0.155116, 0.413160, 0.121601 respectively. Besides Maybank, only HLB is significant towards Z-Score with a lower Z-Score of 0.413160 compare to Maybank. The R-square of the regression model is 0.372297 (i.e. 37.2297 per cent). Based on Model 1, variation in ownership structure can explain 37.2297 per cent of variation in Z-Score. Table 3 presents the regression results on the relationship between ownership structure and Z-Score of the banks.

Table 3: Regression results for the models

Variables	Model 1	Model 2a	Model 2b	Model 2
Intercept	4.042883 (10.36754)***	3.976086 (10.52664)***	3.678782 (2.944383)***	1.461452 (0.945567)
GOVOWN	-0.048552 (-0.095925)	0.125323 (0.102485)	0.305565 (0.214329)	-0.43349 (-0.337958)
FINOWN	-0.617332 (-0.781456)	5.284657 (0.875982)	5.990874 (0.895150)	16.80913 (2.640237)***
BNKOWN	0.256063 (0.439618)	5.549560 (1.339198)	6.123060 (1.287038)	7.584325 (1.744261)*
INDOWN	-0.491610 (-0.496359)	-3.030135 (-1.835006)*	-2.029385 (-0.467916)	-7.941802 (-1.957217)*
MFDOWN	0.245771 (0.491652)	-2.468819 (-2.644122)***	-2.106073 (-1.217850)	-4.667861 (-2.858268)***
GOVOWN*CAR		-0.839412 (-0.090733)	-1.749275 (-0.175101)	-2.142894 (-0.237303)
FINOWN*CAR		-43.10976 (-0.959708)	-47.96483 (-0.975456)	-129.2207 (-2.755992)***



BNKOWN*CAR		-39.20613 (-1.281815)	-43.11120 (-1.249584)	-62.13414 (-1.963240)*
INDOWN*CAR		16.78976 (1.883927)*	10.13735 (0.360746)	45.45233 (1.743677)*
MFDOWN*CAR		19.03084 (3.524590)***	16.72324 (1.560592)	27.04484 (2.711052)***
CAR			1.865227 (0.249771)	-5.348916 (-0.773664)
BNKSZ				0.218571 (3.412340)
LVRG				-0.086690 (-3.524898)
AFFIN	0.190376 (0.852142)	0.291130 (1.418066)	0.284585 (1.367636)	0.625217 (2.718393)***
ALLIANCE	-0.155116 (-0.976790)	-0.149188 (-0.967343)	-0.143321 (-0.913797)	0.180799 (0.923645)
AMMB	0.236173 (1.944866)*	0.372955 (2.948253)***	0.384637 (2.838198)***	0.650738 (4.886291)***
CIMB	0.141758 (1.245185)	0.216455 (2.073827)**	0.218654 (2.076151)**	0.167876 (1.774116)*
HLB	-0.413160 (-3.387100)***	-0.474384 (-4.019306)***	-0.468817 (-3.882539)***	-0.066076 (-0.434482)
PBB	0.247088 (1.019157)	0.223252 (0.933209)	0.232082 (0.954563)	-0.124165 (-0.541171)
RHB	-0.121601 (-1.139849)	-0.040156 (-0.395147)	-0.036382 (-0.352221)	0.284458 (2.447342)**
R²	0.372297	0.529067	0.529412	0.634875



Adjusted R²	0.289524	0.435975	0.429758	0.546893
F-Statistics	4.497761	5.683303	5.312510	7.215980
N	104	104	104	104

The numbers in parenthesis are t-statistic calculated based on robust standard errors. ***, **, *, indicate significance at 1%, 5% and 10% respectively.

The impact of ownership structure on Z-Score with CAR

Model 2

The model has been tested using five ownership structure variables. The F-Statistic (7.215980) suggests that the Model 2 is statistically significant. The coefficients of the ownership structures are such; GOVOWN (-0.433490), FINOWN (16.80913), BNKOWN (7.584325), INDOWN (-7.941802) and MFDOWN (-4.667861). In other words, GOVOWN, INDOWN and MFDOWN have a negative and FINOWN and BNKOWN have a positive relationship with Z-Score. Besides, only FINOWN and MFDOWN are significant with positive and negative relationship with Z-Score respectively. The remaining ownership structures GOVOWN, BNKOWN and INDOWN are not significant towards Z-Score.

The coefficient for interaction variable between ownership structure and capital adequacy ratio (CAR) (GOVOWN*CAR, FINOWN*CAR, BNKOWN*CAR, INDOWN*CAR and MFDOWN*CAR) (t-stat = -0.237303, -2.755992, -1.963240, 1.743677 and 2.711052) is significant at 1 per cent for FINOWN*CAR and MFDOWN*CAR. Thus, one may conclude that CAR has a moderation effect on the relation between ownership structure (FINOWN and MFDOWN) with Z-Score. Capital adequacy ratio, do not has direct impact on the Z-Score as it is statistically not significant (t-stat = 0.773664). Table 3 presents the moderating effect of CAR on the relation of ownership structure variables and Z-Score (Model 2a, Model 2b and Model 2). Bank size (BNKSZ) and Leverage (LVRG) is significant at 1 per cent level (t-stat = 3.412340 and (-3.524898), indicating that bank size and leverage significantly affect the Z-Score.

From this model, Maybank as the reference bank is not significant towards Z-Score. The banks that are significant towards Z-Score are Affin, AMMB and RHB which with higher Z-Score from Maybank by 0.625217, 0.650738 and 0.284458 respectively. As for Alliance and CIMB, the Z-Score are higher than Maybank by 0.180799 and 0.167876, even though both of the banks are not significant to Z-Score. On the other hand, HLB and PBB showed lower Z-Score by -0.066076 and -0.124165 from Maybank and both are not significant to Z-Score.

The R-square of the regression model is 0.634875 i.e. 63.4875 per cent). Based on the Model 2, variation in ownership structure, bank size, leverage and CAR can explain 63.4875 per cent of variation in Z-Score. Comparing the R-square of Model 2 to R-square of Model 1, Model 2a or Model 2b, one can conclude that R-



square has been improved. In other word, Model 2 has more explanation power rather than Model 1, Model 2a or Model 2b.

5. CONCLUSION

Regression results of the first model show that Maybank as the reference bank is significant and has a positive direct relationship with Z-Score. Besides, HLB also is significant but has a negative relationship with Z-Score. In the more complex model that consist of moderating variable, control variables and interaction variables, the result showed there is a positive relationship for Maybank even though is not significant towards Z-Score. In addition, the results show that the Z-Score are higher than Maybank and significant for Affin, AMMB and RHB. Out of the five ownership structure variables, BNKOWN and MFDOWN support the first hypothesis whereby there is a positive relationship between ownership structure and Z-Score, even though there are none of the ownership structure variables significant with Z-Score. As for the second hypothesis, there is a mix finding in term of direction of the relationship and significance on Z-Score when capital adequacy ratio is higher. The result also show that the preferences for risk taking in the commercial banks in Malaysia is affected not only due to the different type of ownership but also due to the moderating factor of capital adequacy ratio regardless of the directions of the relationship.

REFERENCES

- Ahn, S., & Choi, W. (2009). The role of bank monitoring in corporate governance: Evidence from borrowers' earnings management behavior. *Journal of Banking & Finance*, 33(2), 425-434. doi: <http://dx.doi.org/10.1016/j.jbankfin.2008.08.013>
- Altman, E. I. (1968). Financial Ratios, Discriminant Analysis And The Prediction Of Corporate Bankruptcy. *The Journal of Finance*, 23(4), 589-609. doi: 10.1111/j.1540-6261.1968.tb00843.x
- Altman, E. I. (2005). An emerging market credit scoring system for corporate bonds. *Emerging Markets Review*, 6(4), 311-323. doi: <http://dx.doi.org/10.1016/j.ememar.2005.09.007>
- Altunbas, Y., Evans, L., & Molyneux, P. (2001). Bank Ownership and Efficiency. *Journal of Money, Credit and Banking*, 33(4), 926-954.
- Barry, T. A., Lepetit, L., & Tarazi, A. (2009). Bank Ownership Structure, Market Discipline And Risk: Evidence From A Sample Of Privately Owned And Publicly Held European Banks.
- Barry, T. A., Lepetit, L., & Tarazi, A. (2011). Ownership structure and risk in publicly held and privately owned banks. *Journal of Banking & Finance*, 35(5), 1327-1340.
- Beck, T., Demirguc-Kunt, A., & Levine, R. (2003). Bank Concentration and Crises. *National Bureau of Economic Research Working Paper Series, No. 9921*.
- Beck, T., Demirgüç-Kunt, A., & Levine, R. (2006). Bank concentration, competition, and crises: First results. *Journal of Banking & Finance*, 30(5), 1581-1603. doi: <http://dx.doi.org/10.1016/j.jbankfin.2005.05.010>
- Beck, T., Hesse, H., Kick, T., & Westernhagen, N. v. (2009). Bank Ownership and Stability: Evidence from Germany.
- Chu, E. Y. (2004). The Determinants Of ownership Structure In Malaysia.



- Ciancanelli, P., & Reyes-Gonzalez, J. A. (2000). Corporate Governance in Banking: A Conceptual Framework. *SSRN eLibrary*. doi: 10.2139/ssrn.253714
- Demsetz, H., & Lehn, K. (1985). The Structure of Corporate Ownership: Causes and Consequences. *Journal of Political Economy*, 93(6), 1155-1177.
- Dolde, W., & Knopf, J. (2006). Impact of Corporate Ownership and Governance on Risk-Taking and Returns at Thrift Institutions.
- Esty, B. C. (1998). The impact of contingent liability on commercial bank risk taking. *Journal of Financial Economics*, 47(2), 189-218. doi: [http://dx.doi.org/10.1016/S0304-405X\(97\)00043-3](http://dx.doi.org/10.1016/S0304-405X(97)00043-3)
- Galai, D., & Masulis, R. W. (1976). The option pricing model and the risk factor of stock. *Journal of Financial Economics*, 3(1-2), 53-81. doi: [http://dx.doi.org/10.1016/0304-405X\(76\)90020-9](http://dx.doi.org/10.1016/0304-405X(76)90020-9)
- García-Marco, T., & Robles-Fernández, M. D. (2008). Risk-taking behaviour and ownership in the banking industry: The Spanish evidence. *Journal of Economics and Business*, 60(4), 332-354. doi: <http://dx.doi.org/10.1016/j.jeconbus.2007.04.008>
- Gürsoy, G., & Aydoğan, K. (2002). Equity Ownership Structure, Risk Taking, and Performance: An Empirical Investigation in Turkish Listed Companies. *Emerging Markets Finance & Trade*, 38(6).
- Hansmann, H. (2000). *The ownership of enterprise*. T. B. P. o. H. U. P. E. 11-12 (Ed.)
- Iannotta, G., Nocera, G., & Sironi, A. (2007). Ownership structure, risk and performance in the European banking industry. *Journal of Banking & Finance*, 31(7), 2127-2149.
- Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics*, 3(4), 305-360.
- John, K., Litov, L., & Yeung, B. (2008). Corporate Governance and Risk-Taking. *The Journal of Finance*, 63(4), 1679-1728. doi: 10.1111/j.1540-6261.2008.01372.x
- Konishi, M., & Yasuda, Y. (2004). Factors affecting bank risk taking: Evidence from Japan. *Journal of Banking & Finance*, 28(1), 215-232. doi: [http://dx.doi.org/10.1016/S0378-4266\(02\)00405-3](http://dx.doi.org/10.1016/S0378-4266(02)00405-3)
- La Porta, R., Lopez-De-Silanes, F., & Shleifer, A. (1999). Corporate Ownership Around the World. *The Journal of Finance*, 54(2), 471-517. doi: 10.1111/0022-1082.00115
- Laeven, L., & Levine, R. (2006). Corporate Governance, Regulation, and Bank Risk Taking.
- Laeven, L., & Levine, R. (2009). Bank governance, regulation and risk taking. *Journal of Financial Economics*, 93(2), 259-275.
- Lee, K., Lev, B., & Yeo, G. (2008). Executive pay dispersion, corporate governance, and firm performance. *Review of Quantitative Finance and Accounting*, 30(3), 315-338. doi: 10.1007/s11156-007-0053-8
- Levine, R. (2004). The Corporate Governance of Banks: A Concise Discussion of Concepts and Evidence. *SSRN eLibrary*.
- Lum, C. S., & Koh, P. T. N. (2007). Corporate Governance of Banks in Malaysia.
- Mehran, H., Morrison, A., & Shapiro, J. D. (2011). Corporate Governance and Banks: What Have We Learned from the Financial Crisis? *SSRN eLibrary*. doi: 10.2139/ssrn.1880009
- Naceur, S. B., & Kandil, M. (2009). The impact of capital requirements on banks' cost of intermediation and performance: The case of Egypt. *Journal of Economics and Business*, 61(1), 70-89. doi: <http://dx.doi.org/10.1016/j.jeconbus.2007.12.001>
- Nicolò, G. D., & Loukoianova, E. (2007). Bank Ownership, Market Structure and Risk *IMF Working Paper*.
- Pathan, S. (2009). Strong boards, CEO power and bank risk-taking. *Journal of Banking & Finance*, 33(7), 1340-1350. doi: <http://dx.doi.org/10.1016/j.jbankfin.2009.02.001>
- Pedersen, T., & Thomsen, S. (1999). Economic and Systemic Explanations of Ownership Concentration among Europe's Largest Companies. 6(3), 367-381. doi: 10.1080/13571519984133
- Rahman, N. A. A., Ahmad, N. H., & Abdullah, N. A. H. (2012). Ownership Structure, Capital Regulation And Bank Risk Taking. *3rd International Conference On Business And Economic Research (3rd Icerb 2012) Proceeding*.



- Rime, B. (2001). Capital requirements and bank behaviour: Empirical evidence for Switzerland. *Journal of Banking & Finance*, 25(4), 789-805. doi: [http://dx.doi.org/10.1016/S0378-4266\(00\)00105-9](http://dx.doi.org/10.1016/S0378-4266(00)00105-9)
- Saunders, A., Strock, E., & Travlos, N. G. (1990). Ownership Structure, Deregulation, and Bank Risk Taking. *The Journal of Finance*, 45(2), 643-654.
- Shehzad, C. T., de Haan, J., & Scholtens, B. (2010). The impact of bank ownership concentration on impaired loans and capital adequacy. *Journal of Banking & Finance*, 34(2), 399-408.

UKM-Graduate School of Business,
Universiti Kebangsaan Malaysia,
43600 UKM Bangi, Selangor,
Malaysia.



The Effect of Disclosure Corporate Social Responsibility (CSR) Against Corporate Value with Price Earnings Ratio as Moderating Variables on The Main Sectors

MARZUKI

Accounting Departement
Sriwijaya University
INDONESIA

INTEN MEUTIA

Accounting Departement
Sriwijaya University
INDONESIA

inten26@yahoo.com

EMYLIA YUNIARTI

Accounting Departement
Sriwijaya University
INDONESIA

emylia_yuniarti@yahoo.com

Abstract

Corporate Social Responsibility (CSR) is an activity that should be performed by the company for its survival of its company. CSR activities which is done by the company is intended to get more value from the owners of capital. Besides CSR other aspects that can be considered by the investors is the Price Earnings Ratio (PER), which is owned by the company. PER can be used by the investors as a consideration to make the business decisions. The using of CSR as a variable that affects the value of the company based on the stakeholder theory, the theory explains that a company is owned by all the aspects which is related to its company, those are investors, society, and environment. Other theory which support PER is signaling theory, this theory revealed that the company will disclose the information, where the information can add the firm value.

This research used the secondary data which is obtained from BEI. The data tested using the classical assumption test that consist of normality test, multicoleniarity, heteroscedasticity, and autocorrelation. The hypothesis tested by linear regression analysis and moderate regression analysis. The result of the test which is obtained from BEI and based on the results of the test Hypothesis 1 yields a significance of $0.124 > 0.05$ so CSR disclosure has no effect to the firm value. The test to Hypothesis 2 yields a significance of $0.000 < 0.05$ and it's concluded that PER has an influence to the value of the company. Hypothesis 3 yields a significance of $0.039 < 0.05$ and it's concluded that PER is a moderating variable.

The conclusion of this research after testing the data, it can be concluded that H1 is rejected, H2 is received, and H3 is accepted. The result of this research is different with the previous one.

Keywords: Corporate Social Responsibility, Price Earnings Ratio, Firm Value.



1. INTRODUCTION

Nowadays the world is in an era of globalization, the era in which humans no longer have a narrow mind about something, an era of human which almost no longer have either the limiting space and time, it is felt in the business world. The decision taking in a company is not only based on the company's financial performance report but also it's required a report of other aspects in the company. One of the aspect that can be used as a source of evaluation for a company to determine a business decision which is aspects of social business of the company. The activities which done by the company can not be separated from the company's environmental activities. The Company will disclose any information that is considered to increase the value of the company. The disclosure and implementation of Corporate Social Responsibility (CSR) can gain social legitimacy and raise the company's value in a society in a long term (Permanasari, 2010).

Research on Disclosure of Corporate Social Responsibility (CSR) is also carried out by the state oof the world. From research conducted by Helg (2007) in Nigeria can be concluded that the disclosure of corporate social responsibility should adapt to the circumstances of a country from it's culture, economy and so on, it is proven standards set by European and American society is not able to be well received in Nigeria so hopefully there is a standard that is able to summarize the whole things. Research conducted by Belal (2001) in the State of Bangladesh shows that disclosure of corporate social responsibility is still relatively minimal conducted just around 49% of companies which done CSR disclosure and most companies reveal only voluntary. Hall (2002) study conducted in New Zealand where he made 5 companies have a high profile as a sample. Hall concludes that no clear trend of increased corporate social disclosure. It needs a principle as the legal basis which ensures the continuity of social disclosure. Ratanajongkol (2006) study conducted in Thailand, the results of research he did indicate that there is an upward trend overall, but the study shows that the industry also vary depending trend going.

Every company has a purpose. One of the main purpose of the company to increase the value. Companies that have a good value then it will attract investors to invest in the company. Assessment will be undertaken by the investor will determine their investment, investors assess if bad then they will not invest. The main objective of the investor is to invest for the benefit from the company. To get investors who want to make an investment certainly affected by the rise and fall of the value of a company. One of the aspect which can determine the value of the company is the corporate social responsibility. The value of the company can be reflected in the value of company stock which traded by the company in capital market. It is an indicator of the value of the company (Suharli, 2009).

A good company will not put corporate social responsibility as a cost but as an investment in the long run put them into place. Placement of CSR as a long term investment the company will demonstrate a clear commitment and not just aim to look for short term gains, but also thinking about the future, it is in accordance with the accounting principles of going concern. It is good for the survival of the company as well as to increase the company's value in the public evaluation and potential investors. The various things were done by the company can demonstrate that the company is a part of the community and the environment. For the long term the company will get a huge benefit, it just like gain the trust of the public, and minimize conflicts in a certainly time can occur between companies and communities. Instead the company that considers CSR as a mere cost then of course they are not too concerned with the public. The community will automatically do the same thing, so it's very easy to have a friction in the daily life caused by factors both small and large. Based on the description in fact companies that perform activities in the field are still very few who did those things. They tend to pursue short-term gains, but not too concerned about the long term.

Information is a fundamental requirement for investors and potential investors to make decisions. Complete information, as well as the precise time needed by investors in determining business decisions to be taken. As one of the information needed by investors at the moment is information about the corporate social responsibility of the company (Sembiring, 2005).

There are several guidance in CSR Disclosure such as from the Global Reporting Initiative list and the standard that used in this study ISO26000. The ISO26000 is a disclosure standard which published in 2010 covering 7 main aspects, namely organizational governance, human rights, labor, environment, fair business practices, consumer issues, community involvement and development. The main aspect of the entire developed into 37 issue of disclosure. The higher the CSR disclosures by the company it is expected that the company will have the higher



value. This also applies to the opposite lower CSR disclosures by the company it is expected that the lower the value of the company.

This study uses a variable moderating the Price Earnings Ratio (PER). Price earnings ratio is an approach used to influence the value of the company for investment, profit growth, dividend yield (Suharli, 2009). The higher the PER, the higher the price per share of the company is, it causes the company's stock included in the blue chip stocks in the capital market. Although the company has a high stock price and included in the blue chip investors, but more like a low PER stocks. Investors expect at a cheap price then one day it'll go (Margaretha and Irma, 2008). This is consistent with the theory of signal which the information disclosed by the company is a signal to outsiders that have interest for the company. If the company provides a high PER information then the value of the company will also be high. This study uses the price earnings ratio as a moderating variable aims to determine whether PER able to influence the relationship between CSR on firm value.

This study uses primary sector companies data listed in Indonesia Stock Exchange the period 2008-2011. This is due the applied of law principle number 40 of 2007 chapter 74, the application of CSR required for a company engaged in the processing of natural resources. The main sectors of the company is a company which produces raw materials. The company consists of the agricultural and mining sectors, the two sectors are the sectors engaged in the processing of natural resources directly. So that it will be match on the seven major aspects in the guidelines set by ISO26000 as the disclosure of corporate social responsibility. Sector companies which consists of agricultural and mining sectors, a sector which is directly related to nature.

Based on the description above, I conducted research with the title "The Effect of Disclosure of Corporate Social Responsibility (CSR) Against Corporate Value with Price Earnings Ratio as Moderating Variables on The Main Sector".

2. THEORY

2.1 Stakeholders Theory

Stakeholder is an individual, group of people, communities or society as a whole or partially with ties and interests of the company. Based on those people who become stakeholders in a company that has legitimacy, power and the interests of the company (Irawan, 2009).

The Company can be affected by the stakeholders in their activities, even the survival of a company depends on the support it can get. Company should always be looking for support by way of disclosure about what it has done for the company to run its business. Some of the reasons companies consider the interests of stakeholders is the issue of environmental issues which involve the interests of various walks of life that can be a threat to the company if they ignore it. Currently all products traded must pay attention to the environment. More investors have a tendency to invest its capital in companies that give attention to the environmental issues. Non-Governmental Organizations nowadays is increasingly vocal in sounding about the environment and often a critic for the company (Iryanie, 2009).

Under these conditions, the company does not regard the owners of capital in this case only as a creditor and investor stakeholders. Company considers all parties can be based on the interests of stakeholders as well as its legitimacy, the investor has an interest to make a profit, the employees concerned to get a decent wage, the public's interest to get the social services of the agency, including in this case the government can be the stakeholders since the power factor has.

2.2 Legitimacy Theory

Legitimacy theory is a theory that explains that the company is an organization that is legitimate. Organization trying to convince the public that they have done their duty to the environment and to the society. The company also seeks to ensure that operates within the boundaries and norms prevailing in society. Some companies who can do the activities undertaken by the social contract society. Its survival and growth based on:

- a. Giving something a community needs
- b. Distribution of economic benefits to the group that has the power



If one time the company can not fulfill its obligations, then the company may cancel the contract in a way not to use the company's products (Harsanti, 2011).

2.3 Signaling Theory

Signaling Theory is a theory that shows how a company shows an information to the users of the information in this case the financial information of a company. It contains the information about what has been done to realize the objectives of the management shareholders. This information is also used to promote the company shows that the company is better than the other companies (Mungniyati, 2009). This theory is based on the assumption that managers and shareholders do not have the same corporate information. There is information known only to the manager alone while shareholders do not know these things can lead to information asymmetry between managers and shareholders. So whenever there is change in the stock price stockholders also obtain information, thus the value of the company is also subject to change. It has been done to achieve the manager's stock price and profit shares can be used as a signal to shareholders and other external parties (Mulianti, 2010). An information can be said to have value in order for investors to react if such information to perform transactions in the capital market (Cheng and Christiawan, 2011).

This theory indicates that the price earnings ratio as a moderating variable may be a signal to investors in assessing whether a company has a high value or low value, as reflected in the company's stock price. Based on this signaling must be done by the company to get investors to invest in the company. The better the signal that the company is given, the better the reaction of investors. In this case the PER can be used as a signal to investors.

2.4 Corporate Social Responsibility (CSR)

Corporate social responsibility is a concept of organization, which has a responsibility to the shareholders, consumers, governments, communities and environments where the company conducts its business activities, in order to achieve sustainable development (Siahaan, 2008).

The definition of Corporate Social Responsibility (CSR) according to the ISO26000 is "Responsibility of an organization for the Impacts of its decisions and activities on society and the environment, through transparent and ethical behavior that contributes to sustainable development, health and the welfare of society; takes into account the expectations of stakeholders; is in compliance with applicable law and consistent with international norms of behavior; and is integrated throughout the organization and practiced in its relationships. "

There are three categories of Corporate Social Responsibility (CSR) by Susanto (2003), they are:

1. Social Obligation, because the CSR was viewed as one of obligation, then the implementation is generally only meet the minimum requirements set by the government. In this case, no one had the impression in its implementation.
2. Social Reaction, CSR is not only seen as a social obligation, but has begun to grow awareness of the importance of CSR. But for various reasons, the implementation of CSR is still far from the expected, despite being on top just to meet the minimum requirements. In this context, it still needs the external impulses that CSR could be developed further.
3. Social Response, in this phase of the corporation and the community is able to jointly seek opportunities to contribute to the public interest.

Based on the explanation above we can conclude Corporate Social Responsibility (CSR) is the company's attitude toward the public, employees, communities, and the environment that is committed to improving the quality of life in which it has a long-term contribution to the survival of the company relating to employees, the community around the company, as well as environment. This is consistent with legitimacy theory which says that the company has a contract with them.

2.5 Price Earnings Ratio (PER)

Price earnings ratio (PER) is the ratio of share price to net income earned by the firm per share of (Wardani, 2009). Price earnings ratio (PER) is one of the most basic measure of the fundamental stock analysis. Is easy, PER is the



ratio between the share price and net profit of the company, where the price of an issuer's shares compared to net income generated by the issuer within a year. Because the focus of the calculation is the net profit that has generated the company, then by knowing PER an issuer, we can find out whether the price of a stock is considered reasonable or not in real (Hidayat, 2010).

2.6 Corporate Value

Value of company is the basis for investors to invest their capital, in this case the company is focused on valuation of shares owned by the company. For companies that issue shares in the capital of the stock market can be used as a reference for assessing the company. There are several methods that can be used to measure the value of the company, one of them using the market to book ratio. The using measurement of market to book ratio shows the value of a company by comparing the book value and market value (Suharli, 2009).

2.7 ISO26000

ISO26000 is a standard that intended as a guide for companies to undertake social responsibility. These standards govern that should be done in implementing corporate social responsibility. Document ISO 26000:2010 Guidance on Social Responsibility was mainly contains definitions, principles, core subjects and instructions how the principles and core subjects enforced within the organization.

Based on ISO26000 as for the definition of social responsibility is: "Responsibility of an organization for the Impacts of its decisions and activities on society and the environment, through transparent and ethical behavior that contributes to sustainable development, health and the welfare of society; takes into account the expectations of stakeholders; is in compliance with applicable law and consistent with international norms of behavior; and is integrated throughout the organization and practiced in its relationships. "

ISO26000 consists of 7 main aspects of the disclosure can be used as a leading indicator for the company to perform its social responsibility. The seven main aspects are:

- Organizational Governance
- Human Rights
- Employment
- Environment
- Fair Business Practices
- Consumer Issues
- Engagement and Community Development.

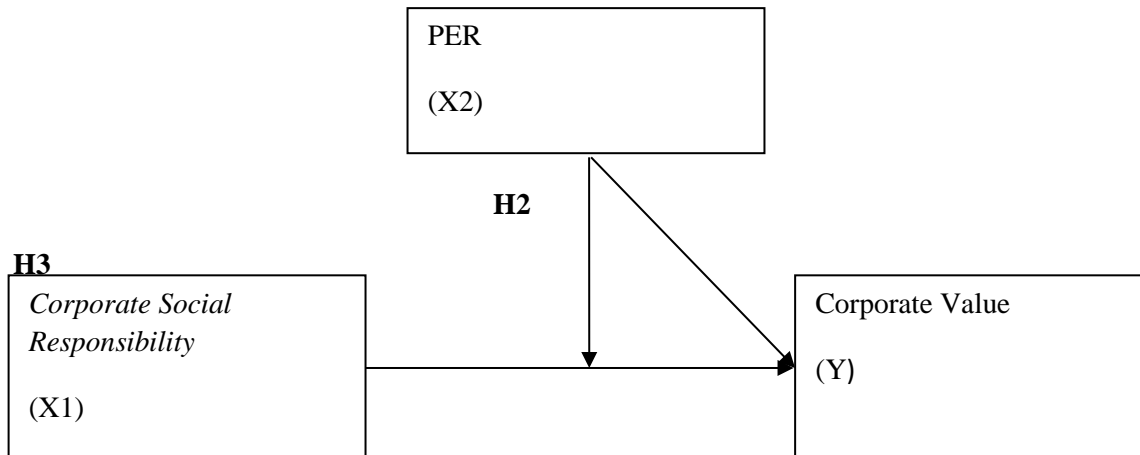
The seven aspects are further developed into 37 issue of disclosure. Issue - the issue which can be used as indicators of the company in carrying out its social responsibility.



3. Research Framework

Based on the discussion above, as well as a literature review of research related to the variables in this study as follows:

Figure 2.1 Framework



H1: Disclosure of Corporate Social Responsibility (CSR) has a positive effect on firm value.

H2: Price earnings ratio (PER) has a positive effect on firm value.

H3: PER has influence as a moderating variable in the relationship between CSR with Corporate Value.

4. RESULTS AND DISCUSSION

4.1 Description of Research Objects

This research uses the object in the form of a public company listed in Indonesia Stock Exchange (BEI), the company posted on the web www.idx.co.id. Public company listed in Indonesia Stock Exchange (BEI) who becomes the object of research is the Primary Sector Company in the year 2008-2011 in accordance with the list of sectors contained in the website IDX.sahamok.com. Primary Sector is the companies listed in Indonesia Stock Exchange (BEI), a sector producing raw materials. Primary sector consists of agriculture and mining sectors. The agricultural sector is divided into several sectors, they are : Livestock sector, plantations, fisheries, and other sectors. The mining sector also consists of several sub-parts sector, the coal mining sector, mining sector, oil and gas, metals and mining sector, other minerals, mining rock - rock and other sectors.

Companies that including to the Sector amounted to 50 companies. (Appendix 1) and using by purposive sampling method with specified criteria. Data of Corporate Social Responsibility (CSR) and financial data is obtained through the Annual Performance Report and Summary of Stock. The Companies sample listed from 2008 to 2011.



Table 4.1 Listed of The Companies

No	Code	Name of the Companies
1	AALI	PT. Astra Agro Lestari Tbk.
2	ADRO	PT. Adaro energy Tbk.
3	ANTM	PT. Aneka Tambang Tbk.
4	BUMI	PT. BUMI Resources Tbk.
5	BYAN	PT. BYAN Resources tbk.
6	CPRO	PT. Central Proteinaprima Tbk.
7	ELSA	PT. Elnusa Tbk.
8	ENRG	PT. Energi Mega PersadaTbk.
9	GZCO	PT. GOZCO Plantation Tbk.
10	ITMG	PT. Indo Tambang Raya Megah Tbk
11	LISP	PT. PP London Sumatera Indonesia Tbk.
12	MEDC	PT. Medco energi International Tbk.
13	PTBA	PT. Tambang Batu Bara Bukit Asam (persero) Tbk.
14	SGRO	PT. Sampoerna Agro Tbk.
15	SMAR	PT. Sinar Mas Agro Resources and Tecnology Tbk.
16	TINS	PT. Timah (persero) Tbk.

Sources : sahamok.com

Data in this research consist of from corporate social responsibility, the price earnings ratio (PER), and Firm Value. To calculate the corporate social responsibility (CSR) using dummy variables derived from company annual reports. Price earnings ratio (PER) was obtained from the Performance Summary of Listed Companies in Indonesia Stock Exchange from the year 2008 to 2011. Values are measured using market to book ratio, market to book ratio can also be obtained directly from the Performance Summary of Listed Companies in Indonesia Stock Exchange from the year 2008 to 2011.

4.2 Data Analysis Results

4.2.1 Descriptive Statistics

Results of testing the descriptive statistics of the variables of Corporate Social Responsibility (CSR), Price Earnings Ratio (PER), as well as the value of the company for the period of observation from 2008 to 2011 are presented in the following table.

Table 4.2 Descriptive Statistics Test Results Statistics

Statistics		CSR_X1	PER_X2	Nilai_Y
N	Valid	64	64	64
	Missing	0	0	0
	Mean	.7204	16.0498	3.0247
	Median	.7297	11.2550	2.3450
	Std. Deviation	.10983	30.14506	3.06360
	Variance	.012	908.725	9.386
	Range	.46	232.05	20.08



Minimum	.43	-80.75	.33
Maximum	.89	151.30	20.41

Sources: Secondary data is processed through SPSS 19

According to descriptive statistics results in the table above, variable Corporate Social Responsibility (CSR) has a value range from 0.43 to 0.89. The lowest value is owned by PT. Gozco Plantation Tbk in 2008, and the highest value is owned by PT. Aneka Tambang (Persero) Tbk in 2010 and 2011, PT. Coal Bukit Asam (Persero) Tbk in 2010 and 2011. Value - average Corporate Social Responsibility (CSR), which is 0.7204. The middle value of 0.7297. Standard deviation of 0.10983 owned. Owned variance of 0.12. CSR value owned by a company is getting its value is close to 1, the more criteria are disclosed ISO26000 company, instead getting closer to 0, the less the company disclosed ISO26000 criteria.

Variable Price Earnings Ratio (PER) has a value range of -80.75 to 151.30. The lowest value is owned by PT. Magnificent Energy Persada Tbk in 2010 and the highest value is owned by PT. BYAN Resources Tbk in 2008. Average value PER is 16.0498. The middle value of 11.2550. Standard deviation value that is owned 20.14506. The variance of the PER 908 725. Price Earnings Ratio (PER) which is owned by a company shows the company's stock price.

Variable Value Company in this study is the dependent variable. Values are measured using market to book ratio. Market to book ratio has a value range of 12.33 to 20.41. The lowest value is owned by PT. Magnificent Energi Persada Tbk in 2008, while the highest value is owned by PT BYAN Resources Tbk in 2010. Value - average market to book ratio, which is 3.0247. The tengah of market value to book ratio which is equal to 2.3450. Standard deviation which is equal to 3.06360 owned and variance equal to the value of 9386. Measurements using the market value of the company to book ratio shows the value of a company, the higher the market value to book value ratio of a company then show the value of company.

4.2.2 Hypothesis 1 (H1) : Correlation between Disclosure of Corporate Social Responsibility (CSR) and Firm Value

Table 4.3 Coefficient of Determination Test Results

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.194 ^a	.038	.022	3.02949

Based on the test results of table 4.3 above shows the determination coefficient R, is the correlation coefficient, shows the R value of 0.194 can be interpreted variable Disclosure of Corporate Social Responsibility (CSR) is not too have a close relationship. R Square has a value of 0.038 or can also mean value of 3.8% can be explained by the variable Value of _YCSR_X1 while the remaining 96.2% was explained by other variables not examined. Value Standard Error of the Estimate (SEE) showed a value of 3.02949 shows the error rate estimation.

Simultaneous Significance Test Results (F Test)

Simultaneous significance test results are presented in Table 4.4 below :

Table 4.4 Simultaneous Significance Test Results
ANOVA^b



Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	22.271	1	22.271	2.427	.124 ^a
	Residual	569.024	62	9.178		
	Total	591.295	63			

a. Predictors: (Constant), CSR_X1

b. Dependent Variable: Nilai_Y

Simultaneous significance test results shows the results of a significance of $0.124 > 0.05$ level. Based on these results it can be concluded that the independent variables simultaneously CSR_X1 not have a significant effect on the dependent variable Value of_Y.

Individual Parameter Significance Test Results (t Test)

Results of individual parameter significance test (t test) are presented in Table 4.5 following:

Table 4.5 Test Results Individual Parameter Significance (t test)

Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.875	2.532		-.346	.731
	CSR_X1	5.413	3.475	.194	1.558	.124

a. Dependent Variable: Nilai_Y

Sources: Secondary datais processedthroughSPSS19

Based on the results of tests of significance of individual parameters indicated by the output of SPSS19 is presented in Table 4.10 shows the result of significance $0.124 > 0.05$ level. Based on these results it can be concluded that there is no significant relationship between the independent variable in this case is CSR_X1 against the dependent variable, that's Value of_Y.

4.2.4 Hypothesis 2 (H2) Correlation Price earnings ratio (PER) and Firm Value.

Table 4.6 Coefficient of Determination Test Results PER

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.436 ^a	.190	.177	2.77899

a. Predictors: (Constant), PER_X2

Based on the table 4.6 coefficient of determination above test results indicate R, is the correlation coefficient, shows the R value of 0.436 can be interpreted variable Price Earnings Ratio (PER) is not too have a close relationship. R Square has a value of 0.190 or can also mean value of 19.0% can be explained by the variable Value of_Y CSR_X1 while



the remaining 81% is explained by other variables not examined. Value Standard Error of the Estimate (SEE) showed a value of 2.77899 shows the error rate estimation.

Simultaneous Significance Test Results (F Test)

Table 4.7 Test Results Statistics F Price Earnings Ratio to Value Company
ANOVA^b

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	112.481	1	112.481	14.565	.000 ^a
	Residual	478.813	62	7.723		
	Total	591.295	63			

a. Predictors: (Constant), PER_X2

b. Dependent Variable: Nilai_Y

Based on Table 4.7 shows the result of statistical tests of significance for F with value $0.000 > 0.05$. The results of the independent variables shows that Price Earnings Ratio (PER) has a significant influence on the variable in this case independent Value of_Y.

Individual Parameter Significance Test Results (t Test)

Result of individual parameter significance test (t test) are presented in the following table below.

Table 4.7 Test Results Statistics t Price Earnings Ratio (PER) to Company Value

Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.313	.394		5.868	.000
	PER_X2	.044	.012	.436	3.816	.000

a. Dependent Variable: Nilai_Y

Based on the test results indicated the significance of individual parameters by SPSS 19 output is presented in Table 4.13 shows the results of significance $0.000 > 0.05$. Based on these results it can be concluded that there is a significant relationship between the independent variable in this case the dependent variable PER_X2 the Value of_Y.

4.2.5 Hypothesis 3 (H3) PER as a moderating variable in relationship between CSR with Corporate Value

The results of hypothesis testing using Moderate Regression Analysis (MRA) is described as follows:

Table 4.8 Determination Test Results

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
-------	---	----------	-------------------	----------------------------



1	.524 ^a	.274	.238	2.67468
---	-------------------	------	------	---------

a. Predictors: (Constant), Moderating_X1.X2, CSR_X1, PER_X2

Table 4.8 shows the amount of Adjusted R Square of 0.238, the value can also be interpreted as 23.8%. The meaning of the value of 23.8% CSR, and Moderation PER explained in terms of company value is measured using Market to Book Ratio. 76.2% while the remaining were explained by cause -other causes outside the model.

Simultaneous Significance Test Results (F Test)

Table 4.9 F Statistic Test Results
ANOVA^b

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	162.060	3	54.020	7.551	.000 ^a
	Residual	429.234	60	7.154		
	Total	591.295	63			

a. Predictors: (Constant), Moderating_X1.X2, CSR_X1, PER_X2

b. Dependent Variable: Nilai_Y

Based on SPSS output is shown in Table 4:9 shows the test results indicate significance of the F statistic $0.000 < 0.05$ it indicates that CSR, and Moderation PER affect the company value in this case is measured by the Market to Book Ratio.

Individual Parameter Significance Test Results (t Test Statistic)

Results of individual parameter significance test (t test) are presented in table 4.8 belows :

Table 4.8 t Test Results

Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.728	3.582		1.320	.192
	CSR_X1	-3.621	5.059	-.130	-.716	.477
	PER_X2	-.489	.253	-4.813	-1.933	.058
	Moderating_PER	.747	.355	5.269	2.107	.039

a. Dependent Variable: Nilai_Y

Based on t-test results shown in Table 4:16 shows the significance value 0.039 Variables Moderating > 0.05 , this thing has a moderating variable showed a significant effect on company value in this case is measured by the Market to Book Ratio. Moderating variable has a value of $0.039 > 0.05$ it shows that PER moderation is moderating variables.

4.2.6 Hypothesis Testing Results

According to the explanations that have been described in Chapter III of this study using a regression equation model to test the hypothesis. There are three hypotheses tested are:



- H1: Disclosure of corporate social responsibility (CSR) has a positive effect on firm value.
 H2: Price earnings ratio (PER) has a positive effect on firm value.
 H3: PER has influence as a moderating variable in the relationship between CSR with Corporate Value.

As for the calculation of linear regression and moderated regression analysis are shown in Table belows :

Table 4:17 Regression Results Calculation and Moderate Linear Regression Analysis

Hipotesis	Equation	Adjusted R ²	Sig. F	Sig. t	Decision
H1	Nilai_Y = -0.875+5.413	0.022	0.124	0.124	Rejected
H2	Nilai_Y = 2.313+0.044	0.177	0	0	Accepted
H3	Nilai_Y = 4.728-3.621 CSR_X1 - 0.489 PER_X2+ 0.747 Moderating_PER	0.238	0.039	0.039	Accepted

Sources: Secondary data is processed

– Hypothesis 1 (H1)

Hypothesis 1 examined the effect of Disclosure of Corporate Social Responsibility (CSR) to the Company's value. Based on the results of measurements of the table 4.17 linear regression revealed a significance level of 0.124 > 0.05. berdasarkan these results, the hypothesis 1 is rejected.

– Hypothesis 2 (H2)

Hypothesis 2 examined the effect of Price Earnings Ratio (PER) of the Company's value. Based on the results shown in Table 4.17 shows the measurement results of linear regression significance level of 0.00 < 0.05. Based on these results, the hypothesis 2 is accepted.

– Hypothesis 3 (H3)

Hypothesis testing price earnings ratio as a moderating variable in the relationship between Pengungkapan corporate social responsibility (CSR) on firm value. Based on the results shown in the table of measurements moderate 4:17 regression analysis showed a significance value of 0.039 > 0.05. Based on these results, the hypothesis 3 is accepted.

5. CLOSING

5.1 Conclusion

Based on the analysis above, we can conclude :

1. The disclosure of Corporate Social Responsibility (CSR) does not significantly affect the value of the company. This is shown by the significant value Disclosure of Corporate Social Responsibility (CSR) of 0.124 > 0.05.
2. Price Earnings Ratio (PER) significantly effect on firm value. This is shown by the level of significance that is owned by the PER for 0000 > 0.05. The results showed that the "PER has a positive effect on firm value" is accepted.

Price Earnings Ratio as a moderating variable has a significant effect on the relationship between the value of the company's CSR disclosure. This is shown by the level of significance that has a value of 0.039 > 0.05. The results showed that the "PER has a moderating effect on the relationship as variabel CSR with corporate value" accepted.



5.2 Limitations

This study has several limitations that may cause disruption to the research results,:

1. It took only sample of primary sector companies listed in Indonesian Stock Exchange which only 16 companies.
2. It using the market to book ratio as a measure of the value of the company. The measurement of companies value can use many methods, so that the market to book ratio may have different results with other measurement tools.

REFERENCES

- Belal, Aatur Rahman. 2001. A Study of Corporate Social Disclosures in Bangladesh. *Managerial Auditing Journal* 16/5 [2001] 274-289
- Bird, Ron et al. 2007. What Corporate Social Responsibility Activities Are Valued by The Market. *Journal of Business Ethic*, No.76 pp 189-206
- Cheng, Megawati dan Yulius Jogi Christiawa. 2011. Pengaruh Pengungkapan Corporate Social Responsibility Terhadap Abnormal Return. *Jurnal Akuntansi dan Keuangan*, Vol. 13, No.1 Hal. 24-36
- Desy. 2012. Penelitian Kolerasional. Diambil pada tanggal 26 November 2012 dari <http://ecaecy.wordpress.com/2012/01/13/penelitian-korelasonal>
- Hall, J.A, 2002, An Exploratory Investigation Into The Corporate Social Disclosure Of Selected New Zealand Companies, School of Accountancy College of Business Massey University.
- Helg, Asa. 2007. Corporate Social Responsibility from a Nigerian Perspective. *Thesis*. Handelshogskolan Vid Coteborgs Universitet.
- Hidayat, Teguh. 2010. Price Earnings Ratio. Diambil pada tanggal 29 Oktober 2012 dari <http://www.teguhhidayat.com/2010/05/price-earning-ratio-dan-price-to-book.html>.
- International Organization for Standardization. 2010. *First Edition : Guidance on Social Responsibility*. ISO26000
- Irawan, Irwan. 2009. Teori Stakeholder. Diambil pada tanggal 10 November 2012 dari <http://irwanirawan.com/2009/06/08/teori-stakeholder/>.
- Iryanie, Emy. 2009. Komiten Stakeholders Perusahaan terhadap Kinerja Sosial dan Kinerja Keuangan. *Tesis*. Program Studi Magister Sains Akuntansi Program Pascasarjana Universitas Diponegoro.
- Kayo, Edison Suta. 2012. Reaslistis Berinvestasi Saham di Buras Efek Indonesia. Diambil pada tanggal 10 November 2012 dari <http://sahamok.com>
- Kompas. 2012. Partisipasi Masyarakat Lemah Picu Konflik. Diambil pada tanggal 18 Desember 2012 dari <http://www.walhi.or.id/id/ruang-media/walhi-di-media/berita-tambang-a-energi/2133-sumber-daya-alam-partisipasi-masyarakat-lemah-picu-konflik.html>
- Margaretha, Farah dan Irma Damayanti. 2008. Pengaruh Price Earnings Ratio, Dividen Yield, dan Market to Book Ratio Terhadap Stock Return di Bursa Efek Indonesia. *Jurnal Bisnis dan Akuntansi* Vol. 10, No.3 Hal. 149-160
- Mapisangka, Andi, Implementasi CSR terhadap Kesejahteraan Hidup Masyarakat, Vol.1, No.1



- Mulianti, Fitri Megah. 2010. Analisa Faktor-Faktor yang Mempengaruhi Kebijakan Hutang dan Pengaruhnya terhadap Nilai Perusahaan. *Thesis*. Program Studi Magister Manajemen Program Pascasarjana Universitas Diponegoro Semarang.
- Mungniyati. 2009. The effect of Corporate governance and Earnings Information On Bond Ratings and Yields, *Jurnal Bisnis dan Akuntansi*, Vol.11 No.2 Hal.129-141
- Nurlela dan Islahudin. 2008. Pengaruh *Corporate Social Responsibility* terhadap Nilai Perusahaan dengan Prosentase Kepemilikan Manajemen sebagai Variabel Moderating. *Simposium Nasional Akuntansi XI*.
- Oktaviandy, Navel. 2011. Variabel -Variabel dalam Penelitian. Diambil pada tanggal 15 July 2012 dari <http://navelmangelep.wordpress.com/tag/pengertian-variabel-penelitian/>.
- Peraturan Pemerintah Republik Indonesia Nomor 47. 2012. Tanggung Jawab Sosial dan Lingkungan Perseroan Terbatas.
- Permanasari, Wien Ika. 2010. Pengaruh Kepemilikan Manajemen, Kepemilikan Institusional, dan Corporate Social Responsibility terhadap Nilai Perusahaan, *Skripsi*. Fakultas Ekonomi. Universitas Diponegoro Semarang.
- Puspito, Ricky. 2012. Macam-macam Variabel dalam Penelitian. Diambil pada tanggal 15 July 2012 dari <http://rickypuspito.blogspot.com/2012/02/macam-macam-variabel-dalam-penelitian.html>.
- Ratanajongkol, Sunee. 2006. Corporate Social Reporting in Thailand. *Qualitative Research in Accounting & Management* Vol. 3 No. 1, 2006 pp. 67-83
- Samuel, Hatane dan Eliato Wijaya. 2008. Corporate Social Responsibility, Purchase dan Corporation Image pada Restoran di Surabaya dari Perspektif Pelanggan. *Jurnal Manajemen Pemasaran*, Vol 3, No. 1, 35-54
- Sembiring, Eddy Rismanda. 2005. Karakteristik Perusahaan dan Pengungkapan Tanggung Jawab Sosial : Study Empiris Pada Perusahaan yang Tercatat di Bursa Efek Jakarta. *Simposium Nasional Akuntansi VIII Solo 15-16 september 2005*.
- Siahaan, Parlungan Gabriel. 2008. Peranan Tanggung Jawab Perusahaan (*Corporate Responsibility*) dalam Pelaksanaan CSR (Corporate Social Responsibility) Terhadap Hak Kesejahteraan Masyarakat. *Jurnal Kewarganegaraan*, Vol 10, PP 37-47
- Suharli, Michell. 2009. Pengaruh Nilai Perusahaan Terhadap *Return* dengan *Price Earnings Ratio* Sebagai Variabel *Moderate*. *Journal of business applied management*, volume 2, No.2, Hal : 7 – 23
- Sun, Zhaoliang and Yuan, Huipeng. 2010. The Relationship between Corporate Social Responsibility and Corporate Value Using the Game Theory. *International Journal of Business and Management*, vol 5 No.9 pp 166-169.
- Suranta, Sri, 2007. Analisis Pengaruh Pengungkapan Informasi Pertanggungjawaban Sosial (*Corporate Social Responsibility*) terhadap *Firm Value* pada Perusahaan Manufaktur di Indonesia
- Susanto, AB. 2003. "Mengembangkan CSR di Indonesia". *Jurnal Reformasi Ekonomi* Vol 4, no. 1 edisi Januari-Desember.



Timothy, Nicolas. 2011. Tiga Perusahaan di Mesuji Janji Lebih Ramah pada Warga. Diambil pada tanggal 18 Desember 2012 dari <http://m.tribunnews.com/2011/12/30/tiga-perusahaan-di-mesuji-janji-lebih-ramah-pada-warga>

Umar, Husein. 2002. *Research Methods in Finance and Banking*, PT GramediaPustakautama : Jakarta.

Ummah, M Bassirun Al. 2009. Jenis – jenis Penelitian. Diambil pada tanggal 26 November 2012 dari <http://basirunjenispel.blogspot.com/>.

Undang-Undang Nomor 40 Tahun 2007 tentang Perseroan Terbatas pasal 74, ayat 1-4

Utomo, Yunanto Wiji. 2012. Ironis, Pembantaian Orangutan. Diambil pada tanggal 18 Desember 2012 dari <http://sains.kompas.com/read/2012/05/04/20365191/Ironis.Pembantaian.Orangutan>

Wardani, Kirana Asih. 2009. Price to Earnings Rasio atau P/E. Diambil pada tanggal 18 July 2012 dari <http://kirana-kontan.blogspot.com/2009/08/price-to-earning-rasio-atau-pe.html>

Wibowo, Agung Edy. 2012. *Aplikasi Praktis Spss dalam Penelitian*. Penerbit Gava Media. Yogyakarta



The Determinant Factors of Indonesian Public Listed Companies' Debt Policy

By

Saiful

Faculty of Economics and Business of Bengkulu University

Abstract

The purpose of this study is to find empirical evidence of the influencing of investment opportunity set, free cash flow, corporate governance, and firm size on debt policy of Indonesian public listed companies. Based on the purposive sampling method, 27 companies or 52 observations were selected as a sample of this study. This study found that investment opportunity set negatively influence to debt policy. It means since the growth of company is high; the agency problem tends to be low, because the companies' free cash flow is low, therefore, the control with debt policy was not needed. This study also found that corporate governance positively influence to debt policy. It means that the better application of corporate governance, the level of debt tend to be high because the company is more believed by the creditor, so that the resource of fund with debt became easier.

Keyword: Investment opportunity set, free cash flow, corporate governance and debt policy

1. Introduction

The purpose of the establishment of the company is to maximize shareholders wealth through the creation of corporate value. In order to achieve these objectives, the company should be managed by professionals. So, the owner of a company that does not have the expertise to manage the company will hire the other parties to become a manager of company. This situation is very common in modern companies where separation between owners and managers is really occur. Separation of owners and managers sometimes has a negative impact on corporate performance. Jensen and Meckling (1976) stated that the conflict of interest between the manager and the owner or agency problems occurs when managers do not control 100% of the shares of the company. Agency problems tend to increase with a decrease in the portion of shares held by managers.



Agency problems can be reduced in several ways, including through the implementation of the debt policy. However, the use of debt policy as a mechanism to reduce or control the agency problem is influenced by several factors, such as the investment opportunity set, free cash flow, corporate governance mechanisms, and firm size. The investment opportunity set indicates the investment companies or growth options. Some study found that the companies with higher growth or investment opportunities will be more likely to use their own funding sources of capital or equity rather than debt. (see for example Gul, 1999; Jaggi and Gul, 1999; Kallapur & Trombley, 2001; Jones & Sharma, 2001). In the context of Indonesian public listed companies, Lestari (2004) mentions that the investment opportunity set negatively affect debt policy, which means that companies that have high growth tend to have lower levels of debt. While Puspitasari and Gumanti (2005) concluded that the investment opportunity set positive effect on debt policy.

Another factor that also affect debt policy is the free cash flow. Jensen (1986) defines free cash flow as remaining cash after the company funded the entire project which resulted in a positive net present value. Companies with excess free cash flow will have a better performance than other companies, because these companies can make a profit over a wide range of opportunities that may not be obtained any other company. Companies with high free cash flow is considered more survive in a bad situation. While the negative free cash flow means internal cash resources are insufficient to meet the investment needs of companies that require additional external funding in the form of debt or the issuance of new shares.

Free cash flow theory predicts that an increase in the amount of debt will increase the value of the company due to agency costs related to free cash flow is likely to decline. Corporate debt can be used to control the use of excess free cash flow (Howton, Howton and Perfect, 1996). Jaggi and Gull (1999) mentions that the free cash flow positive effect on corporate debt policy for the low growth opportunities.

Black, Jang and Kim (2003); Gillan, Hartzell and Starks (2003) and Harford (2005) mentions the existence of a negative relationship between debt policy and the quality of corporate governance. While



Durnev and Kim (2003) actually found that the implementation of corporate governance is positively effect on external funding. Hadrat and Pujiastuti (2007) also stated that the quality of corporate governance has a significantly and positively effect on debt policy.

In addition to the investment opportunity set, free cash flow and corporate governance, firm size is also another factor that affecting corporate debt policy. Several studies provide evidence that supports the positive relationship between firm size and debt policy (Moh'd, Perry and Rimbey, 1998; Brigham and Gapenski, 1999; Soliha and Taswan, 2002). The relationship becomes stronger for larger companies than small firms with low growth opportunities (Jaggi and Gul, 1999).

Because of the inconsistency results of previous studies, this study aimed to examine the effect of the investment opportunity set, free cash flow, corporate governance, and firm size on debt policy in the context of unique emerging markets companies. .

2. Literature Review and Hypothesis Development

2.1. Debt Policy

To funding their operations, the companies can be obtained money from outside the companies (external financing) and from inside the companies themself (internal financing). Internal capital derived from profits, retained earnings and cash flow, while the external capital can come and equity and debt. Growing companies need capital to be gained from debt and equity. The size of the debt ratio can be seen in the ratio of Debt to Asset Ratio. Payable has two advantages, namely (a) the interest paid can be deducted at tax purposes, thus lowering the effective cost and debt, (b) holders of debt(debtholder) get a fixed return (Masdupi , 2005).

The use of debt has the disadvantage because higher debt will be followed by increasing of the risk inturn the interest rates also will be higher as well, and if the condition of the company is not in good condition, operating income is low and not enough to cover the interest costs that property owners are reduced. In extreme conditions, such losses could jeopardize the company because it can be threatened with bankruptcy. To meet the funding needs, wants shareholders over the company financed with debt



financing. Due to the use of debt, their right to the company will not be reduced. But the manager did not like the funding on the grounds that the debts are high risky. Management companies have a tendency to gain profits as the magnitude of the other party (Masdupi, 2005).

Agency problems associated with agency costs can be reduced through some oversight mechanisms such as increasing the use of debt policy, insider ownership and increased dividend payments. In addition, the debt can reduce free cash flow that is excessive. The use of debt will reduce cash flow because the company has to pay interest and principal loan debts that cause a reduction in the money available to the manager. This situation will limit the desire of managers to use cash flow to supplement their income and to invest the excessive (overinvestment). While shareholders want cash flow can be distributed as dividends to increase their wealth or reinvested into projects which generate positive returns. Therefore, the increased use of debt will reduce the agency problem between managers and investors.

High-growth companies have a great opportunity to allow it to pay lower dividends because they have the opportunity to fund profitable investments internally so that companies are not tempted to pay a greater share of profits to outsiders. Conversely a low-growing companies, trying to attract outside funds to finance its investment at the expense of the majority of its profits in dividends and interest. This statement by Fitrijanti and Hartono (2002) are consistent with the predictions of the theory suggesting that companies are growing larger will have lower debt than the company does not grow because he prefers a solution to the problems associated with debt.

2.2. Investment Opportunity Set and Debt Policy

Investment opportunity set (IOS) is the investment opportunity set which is an investment option in the future and reflects the growth of assets and equity. According to Gaver and Gaver (1993), IOS is the value of a company depends on the amount of expenses set forth in the management of the future, which is currently the investment options that are expected to result in a larger return. Investment opportunity



set can not be observed by external parties, so we need a proxy to measure it. According Kallapur and Trombley (2001), in general proxy-proxy IOS can be classified into four types, namely:

1. Proxy based on price
2. Proxy-based investment
3. Proxy-based variant
4. Combination of individual proxy proxy

To minimize the costs incurred in connection with the conflict of interest between managers and shareholders, shareholders include third party to bear the costs of monitoring / surveillance. This is known as the control hypothesis, which is to minimize the actions will benefit themselves taken managers, companies that have high free cash flow with a low growth rate will be more inclined to increase the debt, the logic utilization of available free cash flow is will be invested in projects that have a positive net present value which will increase the value of the company. In this case the manager's actions are restricted by debt covenants set by debtholders.

In contrast to companies that have high growth rates, there will be no problem of agency costs associated with high free cash flow due to the company any excess funds can always be used by the company for growth. Myers (1977) in Lestari (2004) states that companies with high growth rates are more likely to reduce the level of debt. It is associated with higher levels of debt the higher the likelihood the company will be declared bankrupt companies by debtholders if unable to pay the debt. Also stated that companies that have high growth rates are more likely to not add to the debt due to underinvestment and asset-substitution.

In the underinvestment problem, managers are more likely not to invest in projects that have a positive net present value, which may increase the value of the company because it is a party that debtholders have first claim on the cash flows derived from the project. Furthermore, by adding debt,



assets used as collateral owned. Asset substitution problem occurs when managers are opportunistic substitute assets with higher variance variance lower assets, once debts or bonds issued.

In addition to Myers (1977), turned out to Jaggi and Gul (1999) and Bieber (2004) also stated that the investment opportunity set negatively affect debt policy. While Puspitasari and Gumanti (2005) concluded that the positive effect on debt policy investment opportunity set at the end of the expansion stage, mature and decline of the company. Indicating that the level of corporate debt will increase, because the company needs additional funds to invest.

Based on the description and the problem of this study, the first hypothesis is proposed:

H₁: Set the investment opportunity policies negatively affect debt

2.3. Free Cash Flow and Debt Policy

Jensen (1986) defines free cash flow as cash remaining after all projects that generate positive net present value discounted at the relevant cost of capital rate. Free cash flow (free cash flow) is generally described as all cash generated by operating activities can be distributed back to shareholders without affecting the growth rate of the current (and Vahama Jokipii, 2006).

Various conditions can affect the company's free cash flow values. If the company has a high free cash flow with a low growth rate of free cash flow is then supposed to be distributed to shareholders. If the company has a high free cash flow and high growth rate of free cash flow that can be held temporarily and can be used for investments in future periods.

Free cash flow Great managers will lead to wrong behavior and bad decisions, which is not in the interest of shareholders. In other words, the managers have a tendency to use excess profits to consumption and other opportunistic behavior because they receive the full benefits from such activities, but are less willing to bear the risk of costs incurred.

With the debt can be used to control the use of free cash flow excessive by the manager. In addition shareholders will enjoy more control over his management team, for example, if a company issuing new debt and using the proceeds to buy back common shares outstanding, the management is required to pay cash to cover the debt, simultaneously reducing the amount of cash flow available to management to be



mocked. With the existence of the debt, management will work more efficiently in order to avoid financial failure so as to avoid a wasted investment (Jensen (1986).

Agarwal and Jayaraman (1994) in Jaggi and Gul (1999) mentions that the company's free cash flow (FCF) high and low investment opportunity set will have a higher level of debt because debt reduces the agency problems associated with high FCF. Megginson (1997) in Mahadwarta (2002) states that dividend policy affects debt with a positive relationship. Companies that distribute dividends require large amounts of additional funds through debt to finance its investments.

Based on the description and the research problem, the second alternative hypothesis is proposed:

H₂: Free cash flow positive effect on debt policy.

2.4. Corporate Governance and Debt Policy

The concept of corporate governance can be defined as a set of mechanisms for directing and controlling an enterprise that runs the company's operations in accordance with the expectations of the stakeholders. Evolving concept of corporate governance in line with the demands of the public who want the realization of business life healthy, clean and responsible. This demand is actually a public response to the rampant cases of irregularities corporations worldwide.

Forum for Corporate Governance in Indonesia (FCGI) defines corporate governance as "a set of rules governing the relationship between shareholders, corporate managers, creditors, government, employees, and stakeholders internal and external relating to the rights and obligations of their or in other words a system that control of the company ". The main objective of corporate governance is to create added value for all interested parties or stakeholders (FCGI, 2003).

IICG defines corporate governance as the processes and structures that are applied in running the company with the primary objective of enhancing shareholder value over the long term by taking into account the interests of other stakeholders. Corporate governance problems can be traced from the development of agency theory that attempts to explain how the parties involved in the company (managers, company owners and creditors) will behave, because they basically have different interests.



IICG conducted a survey of corporate governance practices adopted by the company and resulted in a score of Corporate Governance Perception Index (CGPI). CGPI measures the extent to which the company meets the rules of corporate governance role in the implementation of seven criteria: (a) the company's commitment to the CG; (B) the implementation of the GMS and the treatment of minority shareholders, including the timely implementation of the GMS and the guarantee of protection of shareholders' rights; (C) the board of commissioners, commissioners had competent in their field and how optimal their roles and responsibilities in the administration of CG; (D) the structure of the board of directors, its directors who are competent in their field and how the roles and responsibilities of directors in the implementation of good corporate governance; (E) the relationship with stakeholders, how relations and corporate responsibility with parties related to the company; (F) transparency and accountability, requiring that the information is open, timely, clear, comparable, especially concerning financial issues, management and ownership of the company; (F) IICG response to the research, the extent of the seriousness of the respondent to follow this research.

Implementation of Corporate Governance (CG) in a company brings many benefits. One of them according to FCGI, by implementing CG, some of the benefits that can be obtained include:

1. Improving the performance of the company through the creation process of making better decisions, improve operational efficiencies and further improve service to stakeholders.
2. Facilitate obtaining cheaper financing funds, which in turn increase corporate value.
3. To enhance confidence of investors to invest in Indonesia.
4. shareholder will be satisfied with the performance of the company as well as to increase shareholder's value and dividends.

In addition to managing the funds of the company's shareholders, corporate managers also manage funds from bondholders or creditors. Conflict of interest between managers and bondholders happen in terms of debt policy. This conflict arises when the management take on projects that have a greater risk than predicted by the lender. In this case the lender would not be harmed if the funds invested in high-risk



projects, because it would increase the risk of bankruptcy of the company, which in turn will affect the value of the company with reduced market value of the debt or bonds that have not matured. Conversely, if a high-risk project that gives good results, the compensation received by the creditor in the form of interest not rise. This suggests that debt can make the transfer of wealth from bondholders to shareholders which will be avoided by the bondholders.

Jensen and Meckling (1976) suggest wearing an increase in the debt to reduce agency costs though for different reasons, namely that outside equity has not increased so that the conflict between outside investors and the management did not increase. Chen and Steiner (1999) concluded that managerial ownership and debt policy has a negative relationship. This is due to the substitution between the two factors. In addition, the high-risk conditions managers select high-risk projects with the objective of achieving high returns. Risk reduction is done by using debt financing from lenders. However, the use of debt at high risk levels can reduce the agency costs of equity but can lead to agency costs of debt.

Black, Jang and Kim (2003); Gillan, Hartzell and Starks (2003) and Harford (2005) suggested a negative relationship between debt policy and the quality of corporate governance. While Durnev and Kim (2003) even mention the existence of a positive relationship will practice corporate elections corporate governance and disclosure to the company's need external funding. Hadrat and Pujiastuti (2007) also mentioned that the quality of corporate governance has a significantly positive effect of the debt policy. This shows that the better the quality of the implementation of corporate governance policies will further increase the debt.

The implementation of better corporate governance makes companies more trusted by lenders, investors and other partners. Therefore corporate funding coming from debt will increase because creditors believed that the company has access to sources of debt funding becomes easier. Although the proportion of corporate debt rose, shareholders would not be worried because the application of the company's corporate governance both will run the principles of transparency, akuntabilitas,



responsibility, independence, and fairness. These principles are used to determine the value IICG Corporate Governance Perception Index (CGPI).

Based on the description and the research problem, the third hypothesis is proposed:

H₃: corporate governance index positively influence debt policy.

2.5. Company size and Debt Policy

According Sujianto (2001) size of a company is demonstrated by total assets, number of sales, the average total sales and average total assets. Firm size is the average total net sales for the year up to several years (Brigham and Houston, 2001:35). In this case the sale is greater than the variable costs and fixed costs, it will obtain the amount of pre-tax income. Conversely, if the sale is less than the variable costs and fixed costs, the company will suffer a loss.

In general, large companies tend to be more diverse and have high levels of bankruptcy or financial difficulty of smaller, it makes them easier access to the capital markets, especially the bond market. Moreover, another important thing that is composed of a large company of Assets-in-place, which makes them able to publish a higher level of debt. Smaller companies are in a weak position to issue debt because of their ability to borrow is limited.

A number of studies have mengemukakan that firm size on corporate debt policy. The bigger the company the more money that is used to run the company's operations and is one source of debt. Large companies can easily access to the capital markets. Ease of access to the capital markets means the company has the flexibility and ability to obtain funds.

Many studies claim that corporate debt policy is influenced by the size of the company and stated there was a positive relationship between firm size and debt ratio. This suggests that companies tend to increase their debts as they grow bigger. The study Moh'd, Perry and Rimbey (1998) found that the size of the firm was positively related and significant effect on debt policy. Relationship becomes stronger for larger companies than small firms with low growth opportunities (Jaggi & Gul, 1999). In addition,



Brigham and Gapenski (1999) in Soliha and Taswan (2002) also states that companies that have high growth rates tend to require funding from external sources is large.

Based on the description and the problem of this research, the fourth hypothesis is proposed:

H₄: Firm size has a positive effect on debt policy.

3. Methods Research

3.1. Operational Definition and Measurement of Variables

3.1.1. Investment Opportunity Set

Investment opportunity set is an investment option in the future and reflects the growth of assets and equity. Investment opportunity set can not be observed by external parties, so we need a proxy to measure it. Sharing of the investment opportunity set proxies have been used by researchers is based on the price proxy, proxy based on investments, proxy or use a proxy-based variant combination of individual proxy.

This research uses a proxy-based measure of prices in the investment opportunity set, namely Market to Book Value of Assets (MBVA). The size of single use proxy for the investment opportunity set is based on the research of Adam and Goyal (2006) which states that the Market to Book Value of the Asset to have better performance with the highest information content in assessing the investment opportunity set than the proxy-proxy for the investment opportunity set other. Market to Book Value of Assets (MBVA) is calculated by the following formula:

$$MBVA = \frac{(\text{Total Aseet}_{it} - \text{Total Equity}_{it}) + (\text{Outstanding Share}_{it} \times \text{Closing Price}_{it})}{\text{Total Asset}_{it}}$$

Where:

MBVA : Market to Book Value of the Asset Companies

Total assets : Total assets owned by the company i in period t

Total Equity : Total equity held firm i in period t

Shares Outstanding : The number of shares outstanding of firm i in period t

Closing Price : Closing share price of firm i at the end of year t



3.1.2. Free Cash Flow

Free cash flow is a company's cash generated from operating activities can be distributed to creditors or shareholders who are not used to working capital or investment in fixed assets. Free cash flow is measured by using the formula Ross, et al (2000) ie subtracting net cash flow from operating activities to net capital expenditures and changes in working capital divided by total assets. The amount of free cash flow ratio is then divided by total assets. The smaller the ratio of the smaller shows free cash flow is used to finance the company's assets. This size is intended to make it more comparable to the firms sampled, so the calculation of free cash flow becomes relative to the size of the company (Rosdini, 2009).

Free cash flow is calculated by the following formula:

$$FCF_{it} = OCF_{it} - (\text{Net capital expenditures}_{it} + \text{changes in working capital}_{it})$$

Where:

- OCF_{it}: operating cash flow of firm i in period t
- Net capital expenditures_{it}: Value of acquisition of fixed assets end - the value of the initial acquisition of fixed assets of firm i at period t
- Working Capital_{it}: The total value of assets - total liabilities of firm i in period t
- Changes in working capital_{it}: Working capital end of year - the beginning of the working capital of firm i in period t

3.1.3. Corporate Governance

Corporate governance can be measured by the size of the board of directors and board of commissioners, the independence of the commissioner, the turnover of directors and ownership structure of the company. In addition, corporate governance can also be measured by an index or rank perusahaan that implement corporate governance (Hadrat and Pujiastuti, 2006). In this study, a measure for corporate governance corporate governance index that uses ranking results to the application of corporate governance in the company, conducted by an independent research institute IICG (The Indonesian Institute for Corporate Governance) and published by Self magazine Sembada. Each item questions raised by IICG has a scale from 0 (lowest quality of its corporate governance) to 100 (highest quality of



its corporate governance), so that the corporate governance index is grouped into three predicate company that is very reliable (a score value of 85 -100), reliable (score of 70 to 84.99 value) and a fairly reliable (score value of 55 to 69.99).

3.1.4. Company Size

Size of company (Firm size) can be expressed in total assets, sales and market capitalization. The greater the total assets, sales and market capitalization greater the size of the company. In this study the size of the company measured using total assets. Firm size (firm size) is calculated by the following formula:

$$FIRM\ SIZE_{it} = Ln\ Total\ Asset_{it}$$

Where:

Ln Total Assets_{it} = Natural logarithm of the total assets owned by the company i in period t

3.1.5. Debt Policy

Measurement of variable debt policy is to use a debt ratio. This size was chosen based on studies Jensen, Solberg and Zorn (1992) which states that the debt ratio emphasizes the importance of debt financing by showing the percentage of assets backed by debt.

The data for policy variable debt is calculated by the following formula:

$$Debt\ Ratio_{it} = \frac{Total\ Debt_{it}}{Total\ Asset_{it}}$$

Where:

Debt Ratio (DR) : The ratio of debt firm i in period t
 Total Debt : The total debt of firm i in period t
 Total Assets : Total assets owned by the company i in period t



3. Population and Sample

The population in this study are all companies listed on the Indonesia Stock Exchange in 2006-2008. Selection of the samples in this study using purposive sampling method with the sampling criteria used are as follows:

1. The company is listed on the Indonesia Stock Exchange in the rating CGPI entry in 2006-2008, published by Self magazine Sembada.
2. Companies included in the ranking CGPI publish financial statements during the period of study is 2006-2008.

If during the observation period, the company entered the ranking CGPI only for one year, then the company is still included in the study sample (pooled data). Based on the above criteria, the obtained sample of 27 companies by the number of observations by 52 observations.

4. Results and Discussion

4.1. Descriptive Statistics

Descriptive statistics are part of the data analysis provide initial gambaran variables used in the study. Descriptive variables used in this study is the average value (mean), maximum, minimum, and standard deviation of each variable. The dependent variable used in this study are presented with the debt policy DEBT and the independent variables used are the investment opportunity set (IOS), free cash flow (FCF), corporate governance (CG) and firm size (SIZE).

Descriptive statistics over the study variables can be seen in Table 4.1 below:

Table 1
Descriptive Statistics

Variables	Mean	Maximum	Minimum	Standard Deviation
DEBT	0.5771	0.91	0.21	0.23407
IOS	1.6719	7.33	0.63	1.10335
FCF	- 0.0468	0.33	-0.66	0.17955
CG	76.9794	89.86	56.38	8.03782



SIZE	29.6907	33.51	22.41	2.13006
------	---------	-------	-------	---------

Sources: Secondary data processed 2010

From table 1 for the entire sample can be seen that of the 52 observations, the average values obtained (mean) and standard deviation for the debt policy (DEBT) is 0.5771 and 0.23407. Standard deviation lower than the mean value indicates that corporate debt policy into this study are relatively similar. The maximum value of 0.91 indicates that the biggest debt ratio of the company and a minimum value of 0.21 which shows the smallest debt ratio of the company.

Variable Investment Opportunity Set (IOS) is a proxy that is used to measure the level of corporate growth opportunities. Opportunity to grow the company can be seen from the investment opportunity. In this study, a proxy for the investment opportunity set that is used is the Market to Book Value of Assets (MBVA). Proxy IOS has an average value and standard deviation of 1.6719 and 1.10335. These results indicate that the companies sampled in this study are not too many investments and investments that do not vary. It can be seen from the comparison of the value of the standard deviation and the average of less than 1 is equal to 1.10335 (1.6719). Maximum value of 7.33 indicates the ratio of the company's investment and a minimum value of 0.63 indicates the ratio of the smallest investment by the company.

Variable free cash flow (FCF) represents the cash issued by companies to finance projects that have a positive NPV is not used for working capital or investment in fixed assets. This variable has an average value of -0.0468 and a standard deviation of 0.17955. Standard deviations greater than the average value indicates that the company's free cash flow into the study varied greatly and save the company more than the proceeds invested in profitable projects, and have a positive NPV. The maximum and minimum values show that the FCF of the company with the largest number of 0.33 and the smallest number is -0.66. Positive direction on the maximum value of FCF indicates that the company's operating cash flow is greater than the amount of net capital and issuing of working capital changes, contrary to the negative direction of the minimum value of FCF indicates that operating cash flow of the company is lower than the amount of net capital expenditures and changes in capital the company's work. The maximum and minimum values showed significant differences in the amount of FCF kept by the company as sample.



Variable scores implementation of Corporate Governance (CG) sample firms have an average of 76.9794%, with a minimum value of 56.38% and a maximum value of 89.86%. This suggests that the quality of the implementation of corporate governance is 56.38% and the lowest quality of the implementation of corporate governance is the highest 89.86%.

Variable size of the company (SIZE) is measured by the natural logarithm of total assets showed an average value of 29.6907, the value of standard deviation of 2.13006 and a maximum value (minimum) of 33.1 (22.41). This shows that the company has total assets of 22.41 smallest and largest companies has total assets of 33.1.

4.2. Univariate Analysis

This analysis was conducted to see the effect of the independent variables and the dependent variable is the individual in a manner to first classify the samples into two groups: companies that have a high IOS and IOS low, companies have negative free cash flow and positive, the company that the application of corporate governancenya quite reliable and very reliable, and small and large companies. This is done to see if there is a difference between corporate debt policies that have a high IOS and IOS are low, debt policies among companies with negative free cash flow positive, debt policies among companies with CG fairly reliable and very reliable, as well as between corporate debt policy large and small and can be seen by the table below:

Table 2
Univariate analysis results Diskriptif

Dependent Variables	Independent Variables	Category	N	Mean	Standard Deviation	t-test
DEBT	IOSCAT	Low	33	0.6694	0.22770	4.361 ***
		High	19	0.4167	0.14243	
DEBT	FCF	Negative	23	0.5295	0.18146	-1316
		Positive	29	0.6149	0.26567	
DEBT	CG	Simply Reliable	19	0.4793	0.16789	-2.539 **
		Highly Trusted	33	0.6366	0.2478	
DEBT	SIZE	Small	27	0.4866	0.20117	-3.140



		Large	25	0.6749	0.23110	

Sources: Secondary data processed 2010

*** Significant at 1% level

** Significant at the 5% level

From Table 2 it can be seen that the debt policy for a group of companies that have a high IOS and IOS has a low average value for IOS DEBT high is 0.4167 and the standard deviation of 0.14243, while the average value for IOS DEBT low is 0, 6694 and a standard deviation of 0.22770. This indicates that the company has a low growth rate of more use of debt of companies that have high growth rates.

DEBT variable for companies that have free cash flow (FCF) has a negative average value and standard deviation of 0.5295 and 0.18146, while the average value and standard deviation for positive free cash flow amounted to 0.6149 and 0, 26 567, which means that the company that has demonstrated positive FCF more use of debt from negative FCF It is intended to reduce the agency problem due to the existence of the debt can be used to control the use of excessive free cash flow by managers.

DEBT variable for companies with the implementation of Corporate Governance (CG) has a fairly reliable average value and standard deviation of 0.4739 and 0.16789, while the average value and standard deviation for the implementation of highly reliable CG is equal to 0.6366 and 0.24798. These results indicate that the level of corporate debt with the application of corporate governance very reliable higher than companies with the implementation of corporate governance is quite reliable. Application of corporate governance which makes the company the better the more trusted by lenders, investors and other partners. Therefore corporate funding coming from debt will increase because creditors believed that the company has access to sources of debt funding becomes easier.

DEBT variable for small firms have an average value and standard deviation of 0.4866 and 0.20117, while the average value and standard deviation for large companies is 0.6749 and 0.23110. These results indicate that large companies have a higher level of debt than small firms because large firms require more funds for the company's operations.

4.3 Hypothesis Testing and Discussion



After testing the classical assumptions, it can be concluded that the data are eligible to proceed to a regression model that can be used to test the research hypothesis.

Table 3
Test Results of Multiple Linear Regression

Independent Variables	Regression Coefficients	t _{count}	Significance
IOS	-0.101	-2.584	0.013 **
FCF	-0.149	-1.222	0.228
CG	0,007	2,266	0.028 **
SIZE	0,010	0.773	0.444
Constant = -0165 F _{count} = 4275 Sig F _{count} = 0,005			

** Significant at the 5% level

Table 3 shows that the investment opportunity set and the negative effect was statistically significant on debt policy. This shows if the company has a high investment opportunity set then companies tend to have lower levels of debt. These results support the opinion of Myers (1977), which states that the company is growing more likely to reduce the level of debt, which is related to the problem underinvestment and asset substitution. In connection with the problem of underinvestment, managers are more likely not to invest in projects that have a positive NPV, because the cash flow from the project will be the first time claimed by creditors. In connection with the problem of asset substitutions, the increase in debt means that most assets of the company will be used as collateral for the debt. In addition to these two problems, Myers (1997) stated that the company grew reduce its debt level to minimize the possibility of claims by creditors if the company can not pay the debt.

The results of this analysis support the statement of Myers (1977) and Holydia (2004) which states that the investment opportunity set negatively affect debt policy. Opportunity set investasi negative effect indicates that the company's high growth opportunities will be more financed with equity capital for investment in the company more profitable and shareholders are likely to want to enjoy the benefits of their own so that the investment would rather be funded with equity rather than debt. These results



conflict with the findings Puspitasari and Gumanti (2005) which states that the debt policy has a positive effect on the investment opportunity set at the end of the expansion stage, mature and decline the company, which means the company will increase the level of debt if the investment opportunity set high because the company needs additional funds to make these investments.

Table 3 also shows that free cash flow does not significantly influence debt policy and its influence is negative. This indicates that companies with high FCF are more likely to use these funds for consumption and corporate managers opportunistic purposes instead of using those funds for investment. So the free cash flow in the study can not be proven as a controller of the agency problem.

The results of this study are not relevant to the research Agarwal and Jayaraman (1994) and Jaggi and Gull (1999) which states that the significant free cash flow and has a positive relationship with the direction of policy loans to large firms with low growth opportunities, which means that the level of debt companies with low growth is high when high free cash flow.

In addition, this study found that corporate governance policies significant positive effect on debt .. These results indicate that the better the quality of the implementation of corporate governance makes companies more trusted by lenders, investors and other partners. Therefore corporate funding coming from debt will increase because creditors believed that the company has access to sources of debt funding becomes easier. In terms of the shareholders, although the proportion of corporate debt increase, they will not be worried because the company that the application of corporate governance that will either run the principles of transparency, akuntabilitas, responsibility, independence, and fairness. So that corporate governance can be proved as controlling agency problems due to the application of corporate governance that better indicate low agency problems.

The results of this analysis are consistent with research Durnev and Kim (2003), Hadrat and Pujiastuti (2007) which states that the quality of corporate governance has a significantly positive effect of the debt policy. These results are not consistent with Black, Jang and Kim (2003), Gillan, Hartzell and



Starks (2003) and Harford (2005) mentions the existence of a negative relationship between debt policy and the quality of corporate governance.

However, this study did not find that the positive effect of firm size on debt policy. Although not significant, but the size of the company have a positive relationship with the debt policy. This indicates that the larger the size of a company would signify more and more funds are needed to fund the company's business activities and one source is the increase in debt. The increase in debt is one of the mechanisms that can control the agency problem because large firms have higher agency problems of small firms. The results of this study are consistent with results of studies Moh'd, Perry and Rimbey (1998), Jaggi and Gul (1999), Brigham and Gapenski (1999) in Soliha and Taswan (2002) which states that the size of the company's positive effect on debt policy.

Goodness of fit Test for Model

F test is used to determine whether the regression model used in accordance (goodness of fit models) . Based on the results of data processing, the value of $F_{\text{calculated}}$ at 4.275 and significance value of 0.005. Value of F_{table} for $k = 4$ $n = 52$ is 2.550. Value $F_{\text{calculated}}$ is greater than the value of F_{table} and significance is less than 0.05 indicates that the regression model made an appropriate regression model, so it can be applied to a population with an error rate of 5%.

The value of the coefficient of determination can be seen in multiple linear regression calculations in table R Square . Based on the results of data processing, the value of Adjusted R Square of 0.208 or 20.8%. This means that the influence of the independent variable is the investment opportunity set, free cash flow, corporate governance and firm size on debt policy (the dependent variable) is only 20.8% while the remaining 79.2% (100% - 20.8%) affected by other variables outside the model of this study. Value Adjusted R Square of 20.8% showed a low effect between the independent variables on the dependent variable in the model for this study more than half are affected by other variables. Adjusted R



Square of low value due to the presence of two independent variables are not significant free cash flow and the size of the company.

5. CONCLUSIONS, IMPLICATIONS, LIMITATION, AND SUGGESTIONS

5.1 Conclusion

The company is seen as a set of contracts between corporate managers and shareholders. The appointment of managers by shareholders to manage the company in fact often face problems due to clash with the company's goals personal goal manager. With authority owned, managers can act to benefit only himself and sacrificing the interests of the shareholders. It is called the agency problem and debt policy is a mechanism that can be used to reduce or control the agency problem.

This study was conducted to obtain empirical evidence about the effect of the investment opportunity set, free cash flow, corporate governance and firm size on debt policy. This study used a sample of companies listed on the Indonesia Stock Exchange and ranking CGPI dilakukan followed by IICG and published by Self magazine Sembada the study period from 2006 to 2008.

Based on the analysis and discussion dikemukakan in the previous chapter, it could be concluded as follows:

1. The results showed that the investment opportunity set significant negative effect on debt policy, it indicates that the higher the investment opportunity set, the lower the level of debt a company has, since growth opportunities more companies funded by equity capital rather than debt.
2. This study did not find that the free cash flow to debt policy. Free cash flow has a negative direction indicates that companies with high free cash flow will have a lower debt level. This indicates that companies with high free cash flow are more likely to use these funds for consumption and corporate managers opportunistic purposes instead of using those funds for investment activities.
3. This study also found that corporate governance significant positive effect on debt policy This shows that the better the quality of the implementation of corporate governance makes



companies more trusted by lenders, investors and other partners. Therefore corporate funding coming from debt will increase because creditors believed that the company has access to sources of debt funding becomes easier.

4. however, this study found no effect of firm size on debt policy

5.2 Implications of Research Results

1. For companies, in conduct that the optimal debt policy considerations influenced the company's growth opportunities and corporate governance. If the company has a high chance of perumbuhan the growth opportunities are more funded with equity capital due to high profit with low risk and the profits tend to want to enjoy themselves by shareholders. If corporate governance, the better the company's corporate debt tends to increase because of easier access to sources of debt funding.
2. For potential investors, with the growth rate of a company determine whether high or low, investors may decide to investing or not. If high growth opportunities, then the investor can invest in companies the benefits are likely to be high with a low risk and benefits can be enjoyed by investors.
3. For creditors, in order to consider the application of corporate governance before giving a loan to the company, ie whether the application of corporate governance of the company can be trusted or not. If the company is to be believed then the lender can give you a loan because the company will not hurt creditors.
4. Strengthen the results of previous studies which stated that the investment opportunity set negatively affect debt policy and corporate governance has a positive effect on debt policy.

5.3 Limitations of Research

1. This study did not include data for the observation period of 2009.
2. This study only measures the investment opportunity set by proxies Market to Book Value of Assets (MBVA).



3. Free cash flow is only measured in one way only so that in the study of free cash flow is insignificant and free cash flow simply grouped into positive and negative.
4. Firm size is measured only by the way just so that the size of the company becomes insignificant in this study.
5. Value of R^2 is lower in this study demonstrate the ability of the independent variables in explaining the dependent variable is limited.

5.4 Suggestions for Further Research

1. Future studies are expected to extend the period of observation as the data index of corporate governance for the year 2009 is available. Researchers can not enter data in 2009 because of the financial report for the year 2009 can not be accessed.
2. Future studies can measure the investment opportunity set with another proxy like proxy based on price, proxied by investment and proxy based variants, and based on the combined proxy. It also connects with the investment opportunity set life cycle of the company.
3. Future studies can measure free cash flow by using other means such as the methods used by Jaggi and Gull (1999) and free cash flow can be classified into high and low, low free cash flow is below the average and above-average height.
4. Future studies can measure firm size by any method as used by Andriyani (2006) is by using the size of the total sales.
5. Future studies may add new independent variables that may affect the dependent variable (policy loans) as the dividend payout ratio and the structure of share ownership.

REFERENCES

- Adam, T dan Goyal, V. K. (2008). The Investment Opportunity Set and Its Proxy Variables. *The Journal of Financial Research*, Vol. 31 No. 1, pp. 41- 63.
- AlNajjar, F. K. dan Belkauoi, A.R. (2001). Empirical Validation of a General Model of Growth Opportunities. *Managerial Finance*. Vol. 27 No.3, pp. 72-88.



- Almilia, L.S dan Silvy, Meliza. (2006). Analisis Kebijakan Dividend dan Kebijakan Leverage Terhadap Prediksi Kepemilikan Manajerial Dengan Teknik Analisis Multinomial Logit. *Jurnal Akuntansi dan Bisnis*, Vol. 6 No. 1, Hal. 1-19 .
- Arifin, Zainal. (2007). *Teori Keuangan dan Pasar Modal*. Yogyakarta: Ekonisia.
- Andriyani, L.N. (2006). Pengaruh Ukuran Perusahaan, Struktur Aktiva, dan Profitabilitas Terhadap Struktur Modal. (Online) (Diakses 27 Desember 2009) Tersedia di situs www.diglib.unnes.ac.id
- Belkauoi, A. R., dan Picur, R. D. (2001). The Investment Opportunity Set Dependence of Dividend Yield and Price Earnings Ratio. *Journal of Managerial Finance*. Vol. 27 No. 3, pp. 65-75.
- Black, B.S., Jang, H., dan Kim, W. (2003). Predicting Firms' Corporate Governance Choices: Evidence from Korea. Working Paper- <http://papers.ssrn.com/abstract=428662>.
- Brigham dan Houston. (2001). *Dasar-Dasar Manajemen Keuangan Buku II*. Edisi ke sebelas. Terjemahan oleh Ali Akbar Yulianto. (2006). Jakarta: Erlangga
- Chen, R. Carl dan Steiner, T.L. (1999). Managerial Ownership and Agency Conflict : a Nonlinear Simultaneous Equation Analysis of Managerial Ownership, Risk Taking, Debt Policy and Dividend Policy. *Financial Review*, Vol. 34 No. 9, pp. 19-137.
- Chung. (1993). Assets Characteristics and Corporate Debt Policy. *Journal of Bussiness Finance and Accounting*, Vol. 20 No. 4, pp. 83-98.
- Crutclely, C dan Hansen. (1999). A Test of The Agency Theory of Managerial Ownership, Corporate Leverage and Corporate Dividends. *Journal of Financial Management*, Vol. 18 No. 3, pp.34-36.
- Durnev, A. dan Kim, E. H. (2003). To steal or Not to Steal: Firm Attributes, Legal Environment, and Valuation. *The Journal of Finance*. Vol.9 No.3, pp. 1461- 1493.
- Fitrijanti, T., dan Hartono, J. (2002). Set Kesempatan Investasi : Konstruksi Proksi dan Analisis Hubungannya Dengan Kebijakan Pendanaan dan Dividen. *Jurnal Riset Akuntansi Indonesia*. Vol.5 No.1, hal.35-63.
- Forum for Corporate Governance in Indonesia. (2003). *Corporate Governance : Tantangan dan Kesempatan bagi Komunitas Bisnis Indonesi*. Jakarta: PT Prenhallindo.
- Gaver, J.J., and Gaver, K.M. (1995). Compensation Policy and the Investment Opportunity Set. *Financial Mngement*. Vol. 24 No. 1, pp. 19-32.
- Ghozali, Imam. (2005). *Aplikasi Analisis Multivariate dengan Program SPSS*. Semarang: Badan Penerbit UNDIP.
- Gillan, S.L.; Hartzell, J.C.; dan Starks, L.T. (2003). *Industries, Investment Opportunities, and Corporate Governance Structures*. Working Paper.
- Gujarati, Damador. (1997). *Ekonometrika Dasar*. Terjemahan Sumarno Zain. (2006). Surabaya: Erlangga.



- Lestari, Holydia. (2004). Pengaruh Kebijakan Hutang, Kebijakan Dividen, Risiko dan Profitabilitas Perusahaan Terhadap Set Kesempatan Investasi. Makalah disajikan pada SNAVII, Denpasar.
- Howton, S.D., Howton, S.W., dan Perfect, S.B. (1996). The Market Reaction to Stright Debt Issues: The Effects of Free Cash Flow. *The Journal of Financial Research*, Vol. 21 No. 2, pp. 219-228.
- Hutchinson, M dan Gull, F.A. (2004). Investment Opportunity Set, Corporate Governance Practice and Firm Performance. *Journal of Corporate Finance* Vol. 10 No. 5, pp. 595-614.
- Indrianto, Nur dan Supomo, Bambang. (2002). Metodologi Penelitian Bisnis untuk Akuntansi dan Manajemen. Edisi Pertama. Yogyakarta: BPF.
- Jaggi, B., dan Gul, F.D., (1999). An Analysis of Joint Effects of Investment Opportunity Set, Free cash Flow and Size on Corporate Debt Policy. *Review of Quantitative Finance and Accounting*, Vol. 12 No. 1, pp. 371-381.
- Jensen, M.C. (1986). Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers. *AEA Papers and Proceedings*, Vol. 76 No. 2, pp. 323-329.
- Jensen, Solberg dan Zorn. (1992). Simultaneous Determination of Insider Ownership, Debt and Dividend Policies. *Journal of Financial Economics*, Vol. 27 No. 2, pp. 305-360.
- Jokipii, A dan Vahamaa, S. (2006). The Free Cash Flow Anomaly Revisited: Finnish Evidence. *Journal of Business & Accounting*, Vol. 33 No. 7, pp. 961-978.
- Kallapur, S. dan Trombley, M.K., (2001). The Investment Opportunity Set: Determinants, Consequences and Measurement. *Managerial Finance*. Vol. 27 No. 1, pp. 3-15.
- Masdupi, Erni, (2005). Analisis Dampak Struktur kepemilikan pada kebijakan Hutang dalam Mengontrol Konflik Keagenan. *Jurnal Ekonomi & Bisnis Indonesia*. Vol. 20, No. 1, hal 57-69.
- Moh'd, M.A., Perry, LG., Rimbey, JN. (1998). The Impact of Ownership Structure on Corporate Debt Policy: a Time-Series Cross-Sectional Analysis. *The Financial Review*, Vol. 33 No. 6, pp.85-98.
- Puspitasarai, Novi dan Gumanti, T.A. (2005). Investment opportunity Set, Resiko dan Kinerja Finansial Dalam Tahapan Siklus Kehidupan Perusahaan Publik di Indonesia Tahun 1999-2003. Makalah Disajikan Pada Simposium Riset Ekonomi II, Surabaya.
- Rosdini, Dini. (2009). Pengaruh Free Cash flow Terhadap Dividen Payout Ratio. Working Paper in Accounting and Finance, Universitas Padjajaran.
- Salman dan Farid. (2007). Pengaruh Karakteristik Perusahaan dengan Faktor Regulasi sebagai Variabel Kontrol Terhadap Kualitas Good Corporate Govenance Perusahaan. *Jurnal Ventura*, Vol. 10 No. 2, hal 1-14.



- Sayidah, Nur dan Pujiastuti, Diah. (2007). Corporate Governance dan Rasio Hutang Perusahaan. Working Paper.
- Soliha, E dan Taswan. (2002). Pengaruh Kebijakan Hutang Terhadap Niali Perusahaan Serta Beberapa Faktor Yang Mempengaruhinya. Jurnal Bisnis dan Ekonomi, Vol. 8 No. 5, Hal. 1-17.
- Sugiyono. (2006). Metode Penelitian Bisnis. Edisi Keenam. Bandung: Alfabeta.
- Sujianto, Agus Eko. (2001). Analisis Variabel-Variabel Yang Mempengaruhi Struktur Keuangan Pada Perusahaan Manufaktur Yang Go Public di Bursa Efek Jakarta. Jurnal Ekonomi dan Manajemen Universitas Gajayana Malang, Vol. 2 No. 1, Hal. 125-138.



The Influence of Internet Financial Reporting and Degree of Information Disclosure on Company's Website to the Frequency of Stock Trading on Trading, Services, and Investment Company Listed on Indonesian Stock Exchange

YULIA SAFTIANA
Accounting Departement
Sriwijaya University
INDONESIA
ysaftiana@yahoo.com

SAVITRI DEWI WULANDARI
Accounting Departement
Sriwijaya University
INDONESIA

EMYLIA YUNIARTI
Accounting Departement
Sriwijaya University
INDONESIA
emylia_yuniarti@yahoo.com

RELASARI
Accounting Departement
Sriwijaya University
INDONESIA
relasari_mkr@yahoo.co.id

Abstract

Development of information technology, especially internet, has affected the traditional form of presenting information on company. An additional media appears to present financial report through the internet or website, it is called Internet Financial Reporting (IFR). Furthermore, company began an effort to reduce the asymmetry of information by utilizing the company's website to disclose information related to the company. This research aims to determine the effect of IFR practices and the disclosure of information on the company's website to the frequency of trading stock on trading, services, and investment company.



This research uses data collected in 2009-2011. Linear regression is used to determine the correlation between IFR and the degree of information disclosure on the company's website to the frequency of trading stock on trading, services, and investment company.

The results of this research indicate that the IFR and the degree of information disclosure on the company's website have positive effect to the frequency of trading stock on trading, services, and investment company.

Keywords: Internet Financial Reporting, degree of disclosure, information disclosure on the website, financial reporting disclosure, the frequency of stock trading.

INTRODUCTION

In recent decades the development of technology is growing rapidly, especially in the field of communications. This development of technology has brought changes not only in the public mindset, but also how a company's business and how information is exchanged. One of the biggest developments in information field and communication technology is the development of the Internet.

According to Internet World Stats on its website www.internetworldstats.com, in the last ten years the number of Internet users in the world continues to increase. From 300 million users in 2000 increased to 2 billion users in 2011. In Indonesia, Internet users reached more than 39 million to the end of 2011. (Source: www.internetworldstats.com).

The development of technology in the business world is shown by many companies have their own personal website. The company uses a website to disseminate not only financial information but also non-financial information. Financial disclosure in the company's website (Internet Financial Reporting-IFR) is a form of voluntary disclosure that have been practiced by various companies. 1000 survey of large European companies showed that 67% of companies already have websites and 80% of companies that have a website on the internet reveals the financial statements. By 2006, more than 70% of large companies in the world adopted IFR (Kahn, 2006).

In Indonesia, Bapepam issued a regulation through the Chairman Decree No.86 of 1996 regarding the disclosure of information that must be announced to the public which reads: "Every public company or issuer that the registration statement has become effective, needs submit to Bapepam and make public as soon as possible, most later than the end of working day-2 (two) after the decision or the presence of material information or facts that may affect the value of corporate securities or investment decisions investors ".

According to Samsul (2006), the principle of information disclosure is very important for capital market participants, especially the public investors either good or bad information that could affect the running of the company have reached the hands of public investors. Capital market participants will evaluate any announcements published by issuers, so that it will cause some changes in the stock trading, such as price changing, volume, and frequency of stock trading. This indicates that the information coming into the market will trigger a reaction from the capital market. This is consistent with signaling theory, where the stock price, volume, and frequency of stock trading that forms in the market is a reflection of existing information. (Ball & Brawn, 1968; Fama et al., 1969).



In this study, the frequency stock trading used to determine the relationship between information and stock. Logically, the more information is circulated, the more demand and supply that led to the transaction by the investor that would trigger an increase in the frequency of stock trading.

This research refers to previous research conducted by Hargyantoro (2010), the influence of internet financial reporting and disclosure level on the frequency of stock trading website. Companies that take are listed in the index compass 100 in 2009 while this study examined the influence of internet financial reporting and degree of information disclosure on company's website to the frequency of stock trading on trading, services, and investment company in the research period of 2009-2011. Meanwhile, the reason why researcher took trading, services, and investment company as the object of research is based on the information contained in the Factbook IDX trading company, services, and investment is a company with the largest number of listed company that have their own website until the end of 2011.

Based on the description above, this study took the title "The Influence of Internet Financial Reporting and Degree of Information Disclosure on Company's Website to the Frequency of Stock Trading on Trading, Services, and Investment Company Listed on Indonesian Stock Exchange "

Problem Statement

1. Does Internet Financial Reporting (IFR) affect the frequency stock trading on trading, services, and investment company?
2. Does the degree of information disclosure on company's website affect the frequency of trading company stock trading, services, and investment?

LITERATUR REVIEW

Signalling Theory

Signaling theory explains why the company has the urge to provide financial information to external parties. Urge companies to provide information is to reduce information asymmetries between firms and outsiders. Lack of external information about the company caused them to protect themselves by providing low prices to the company. Companies can increase firm value by reducing information asymmetry. One of is to give a signal to outsiders, namely in the form noted that financial information is reliable and will reduce the uncertainty about the future prospects of the company (Wolk et al., 2000 in Sari & Zuhrotun, 2006).

Marston (2003) states there is a general perception that the management company that performs well in more open with information than the management of poorly performing companies. Based on signal theory, in such situations the harder to improve the management of shareholder confidence and support of management contracts. Marston also states that profitable firms will have more financial resources to comply with additional disclosure. So, the more profitable a company, the greater the possibility for them to disclose additional financial information.

Disclosure of Financial Statements



According to Warren et al. (2008) financial statements are accounting reports that yield information about the state of a company as well as a communication tool between the company's information with interested parties with company's information. Complete financial report normally includes a balance sheet, income statement, statement of changes in financial position (which can be presented in various ways such as a cash flow statement), and the records of the financial statements.

a. Mandatory Disclosure

Mandatory disclosure is a disclosure made by companies about important information concerning the activities of companies in real terms and conditions that are mandatory and set out in regulations (Suwardjono, 2005 in Kusumawadini, 2010).

According to the Decree of the Chairman of Bapepam. Kep-38/PM/1996 dated January 17, 1996, companies that have made public offerings and public company is obliged to submit an annual report containing the Financial Highlights, analysis and discussion by Management, audited Financial Statements and Management Report. Financial statement submitted must be prepared in accordance with Accounting Principles Thanking General (GAAP) established by the Institute of Accountants Indonesia and Bapepam regulations in the accounting field and have been audited by an Accountant registered with Bapepam. Along with the development regulations in the business world is enhanced in the Decision of the Chairman of Bapepam-LK. Kep-134/BL/2006.

b. Voluntary Disclosures

Voluntary disclosure is a disclosure made by the company beyond what was required by accounting standards or regulatory oversight body.

Easley & O'Hara (2004) stated that the company reserves the right to provide additional information to facilitate voluntary users of financial statements in making decisions. Extensive voluntary disclosure depends on company policy. Among the company's policy and the other one will be different. This is due to the lack of extensive regulations regarding voluntary disclosure, so not all companies do the same disclosure practices, but according to the needs of the company.

Internet Financial Reporting (IFR)

Internet Financial Reporting is the inclusion of financial information via the internet or the company's website (Lai et al., 2010). Venter (2002) in Kusumawadini (2011) suggests that there are three ways of presentation of financial statements through the website, namely:

1. Make a duplicate of financial statements that have been printed to paper in electronic format.
2. Converting financial statements into HTML format.
3. Increase the inclusion of financial statements through the website so that it more accessible by interested parties rather than the financial statements in print format.

Fitriana (2009) in Kusumawadini (2011) revealed that the IFR has several advantages, among others:

1. Offers a low cost solution for both parties.



2. Offers timeliness in the dissemination of and access to information so that information is more relevant as time.
3. As the mass communication media to report the company.
4. Offers financial information in a format that facilitates sharing and can be downloaded. Adobe Acrobat format in portable document format (PDF) is usually the most common format used (Pervan, 2006). In addition to the format used is HTML (Hypertext Markup Language), Excel.
5. Allows the user to interact with the company to inquire or order specific information in a way that is much easier and cheaper.

Frequency Trading Shares

Frequency is the number of times stock trading transactions in question occurred in stock at any given time. With the stock trading frequency is known stock investor is interested or not. The more the frequency of trading a stock means the stock is more liquid. Conversely, if the stock is trading a little mean frequency of these shares are not liquid or unattractive to investors (Samsul, 2006).

Stock trading frequency greatly affect the number of shares outstanding, if the amount of the stock trading frequency is stated as the most active stocks traded and indirectly affect the volume of stock trading. Frequency of large trades of shares of stock transactions allegedly influenced a very active, and this is because many investors. An increasing demand for the shares will indirectly increase the frequency of trading (Samsul, 2006).

Research Accomplished

Development of empirical research related to Internet Financial Reporting (IFR), which reflects the development of corporate disclosure forms began to grow rapidly since 1995. In general, this study focuses on the more developed countries, like Britain, the United States, Germany, Australia, Japan, and China. As for the newly developing countries there is some research on the Internet Financial Reporting.

Several previous studies related to information associated with the following proposed IFR. Ashbaugh et al. (1999) conducted a survey of 290 U.S. companies have traditionally its financial reporting practices have been evaluated by the AIMR. The hypothesis proposed in this study is the size of the firm, ROA, reporting by the AIMR rankings, and the percentage of shares held by individual investors against the IFR. Of testing showed that only the size of the companies that have a significant effect on financial reporting practices through the internet.

Marston (2003) conducted a study on IFR practices in Japan. This study examined the relationship between firm size, industry type, profitability and overseas listing status of IFR practices in Japan. The results show there is a positive relationship between firm size to IFR. While the type of industry, profitability and overseas listing status had no effect on IFR practices in companies in Japan.

Lai et al., (2010) examined the quality of IFR and concluded that the quality was positively related to firm size is expressed in the form of stock ownership or capitalization of the company.

Research related to Internet Financial Reporting in Indonesia itself has started being conducted by several researchers. Among them done by Chariri & Sustainable (2005), Budi & Almilia (2007), Chandra (2008), Almilia (2009), Sharon (2009), and Hargyantoro (2010).

Chariri & Sustainable (2005) conducted measurements of the seven factors that affect the IFR (company size, profitability, liquidity, type of industry, leverage, auditor reputation, and age of listing the company). The result is a positive effect on IFR is firm size, liquidity, leverage, auditor reputation, and the age of the listing companies.



Budi & Almilia (2007) measure the quality of Financial and Sustainability Reporting on the website of the bank sector and LQ-45, whereas Almilia (2009) analyzed the quality of the content of financial and sustainability reporting in publicly traded companies that concluded that companies in Indonesia have not been optimally utilize the website for disclose the information.

Chandra (2008) investigated the influence of company size, profitability, leverage, liquidity, public ownership, foreign ownership, listing age of the inclusion of financial information on the website. The result of company size, public ownership and foreign ownership have a significant effect on the inclusion of financial information on the website.

Fitriana (2009) investigated the influence of competition, firm size, profitability, leverage of wider disclosure of financial information on a company website. The results obtained are only firm size and leverage a significant effect on the area of financial disclosure in the company's website.

Hargyantoro (2010) tried to connect the IFR and the level of disclosure on the website of the frequency of trading in shares in companies that enter into the compass 100 index, a result both have a significant influence on the frequency of stock trading.

Hypothesis

H1: Internet Financial Reporting has positive effect on the frequency of stock trading on trading, services, and investment company.

H2: The degree of information disclosure on the company's website has positive effect on the frequency of stock trading on trading, services, and investment company.

METHODS

Scope of Research

In writing this paper, the authors limit the scope of the discussion only on the frequency aspect of stock trading in the company's trade, services, and investments are listed on the Indonesia Stock Exchange between the years 2009-2011.

Draft Research

Types of research used in this study was descriptive statistics and the study is quantitative.

Data Sources and Collection Techniques

Source of Data

The data used in this study is secondary data, ie data obtained from the indirect object, but rather by way of search-related data objects under study, for example through the books or documents deemed relevant (Cooper & Emory, 2004) . Secondary data used in this study is the financial and non financial information contained in the company's website and stock trading frequency obtained from the IDX Factbook 2009-2011.

Data Collection Techniques

1. Field Research.

That is, with documentation in the form of data collection techniques in Indonesia or the Indonesia Stock Exchange Stock Exchange (IDX) of the years 2009-2011.

2. Library Research

Namely data collection as well as the theoretical basis of previous studies obtained from books, internet, journals, and other written sources relating to the information needed.



3. Recording of relevant information through the company website.

Measurement of IFR and Disclosure Levels

Methods for measuring the level of application of the information was adapted from a study conducted by Ettredge et al. (2001) in Lai et al. (2010) by incorporating the basic profile and operational items. Measurements using a 4 point scale. Profile of the company is given a value of 1, a brief financial report is given 2 points, a complete financial report is given 3 points, and annual reports of directors including the company's business strategy, objectives and business plan are given points 4. Total points ranged from 0-40.

To measure the IFR refers to the practice of application of research Supriadi (2010) a scoring table on the annual financial statement information evaluation criteria are based on GAAP and Bapepam regulations. Total maximum points that can be obtained is 81.

The measurement does not use the nominal scale, but using the index, ie by dividing the points obtained by each company with a total maximum points. For the disclosure of information on the website and the denominator is 40 for IFR practice of application of this denominator is 81.

Population and Sample

This study population is a trading company, services, and investments are listed on the Indonesia Stock Exchange in 2009-2011. Until the end of 2011 there were 87 companies listed on the Stock Exchange. To determine the amount of sample that is by using a calculation formulated by Slovin (Cooper & Emory, 2004). The formula used is as follows:

$$n = N / (1 + Ne^2)$$

Where:

n = number of samples

N = total number of members of the population

e = error tolerance (tolerance of error; significance level; typically 0.05)

² = squared

From the formula above, the calculation to determine the number of samples in this study were:

$$n = N / (1 + Ne^2) = 87 / (1 + 87 \times 0.05 \times 0.05) = 71 \text{ companies.}$$

Based on the above then this study used a sample of 71 companies taken using simple random sampling method.

Operational Definition and Measurement of Variables

This study uses two types of variables. The independent variable in this study is the Internet Financial Reporting-IFR (X1) and the level of disclosure on the website (X2) while the dependent variable in this research that shares trading frequency (Y).

1. Independent variable.

Independent variable is a variable that affects the other variables. The independent variable in this study, namely Internet Financial Reporting (X1) and the level of disclosure on the website (X2).

2. Dependent variable.



Dependent Variable is a variable that is bound to be influenced or caused because of the independent variables. Dependent variable in this research that the frequency of stock trading. Frequency is the number of times stock trading transactions in question occurred in stock at any given time.

Analysis Techniques

This study uses a quantitative approach. Analysis tools used in this study were multiple linear regression. Some of the steps taken in the linear regression analysis are described as follows:

Descriptive Statistics

Intended that the presentation of descriptive statistics can be seen the profile of the research data with the existing relationship between the variables used in the study. In this study the variables used are Internet Financial Reporting (IFR), the disclosure of information on the company website, and the frequency of trading company stock trading, services, and investment.

Regression Model

Analysis tool used is multiple linear regression analysis is used to see the influence of IFR practices and level of disclosure of information on the company website to the frequency of stock trading. Data processed with the help of SPSS software. Regression equation model as follows:

$$Y = a + b_1X_1 + b_2X_2 + e$$

Where:

Y = frequency of stock trading

a = Constant

X1 = Practice IFR

X2 = level of disclosure of information on the website

b1 = regression coefficient IFR Practice

b2 = regression coefficient on the level of disclosure of Information website

e = error

Tests of Hypotheses

Individual Parameter Significance test (t statistics test)

T statistical test basically shows how far the influence of individual independent variables in explaining the variation in the dependent variable. T statistical test was used for to obtain reasonable assurance about the goodness of the regression model in predicting.

ANALYSIS AND DISCUSSION

Descriptive Statistics

From the collection of secondary data regarding the application of the IFR, the level of disclosure in the company's website, and the frequency of trading in the company's shares trade, services, and investment in 2009-2011, the descriptive statistics, namely the minimum, maximum, mean, and standard deviation of study variables were as the following:



Descriptive Statistic Table Result

	N	Minimum	Maximum	Mean	Std. Deviation
Praktik_IFR	213	.395	.962	.66240	.180399
Pengungkapan_Informasi	213	.075	.950	.48897	.268164
Frekuensi_saham	213	10.000	443.000	209.47418	98.838899
Valid N (listwise)	213				

From the table above, can be explained that the average IFR variables (X1) is the standard deviation of 0.66240 to 0.180399, and the amount of existing data 213. IFR minimum value for the variable is 0.395 and the maximum value is 0.962. For the disclosure of information on the company website (X2), the average value is 0.48897 with a standard deviation of 0.268164 and the amount of data is 213. Minimum value obtained is 0.075 and the maximum value of 0.950. The average frequency of trading stock (Y) is 209.47418 98.83889 times the standard deviation and the amount of data as much as 213. Minimum value obtained was 10 times and the maximum value is 443 times.

Regression equations

Regression Test Results Table

Model		Unstandardized Coefficients		t	Sig.
		B	Std. Error		
1	(Constant)	274.473	53.176	5.162	.000
	Praktik_IFR	328.114	149.884	2.189	.003
	Pengungkapan_Informasi	311.562	100.830	3.090	.002

a. Dependent Variable: Frekuensi_saham

From the table above can be used to determine the relationship between the practice of application of the IFR and the disclosure of information on the website of the frequency of stock. Practice application of IFR (Praktik_IFR) as independent variables (X1), the disclosure of information on the company website (pengungkapan_informasi) as the independent variable (X2), and frequency of trading stock (frekuensi_saham) as the dependent variable (Y). From the table above can be arranged in the following equation:



$$Y = 274.473 + 328.114 + 311.562 X_1 X_2$$

Test of Hypothesis

Partial test (t-test)

Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	274.473	53.176		5.162	.000
Praktik_IFR	328.114	149.884	.599	2.189	.003
Pengungkapan_Informasi	311.562	100.830	.845	3.090	.002

a. Dependent Variable: Frekuensi_saham

T seen a test of the significance of each variable. If the value of sig. <0.05 then each independent variable affects the dependent variable.

Based testing has been done, it appears that praktik_IFR variables have a significance value of 0.003 means that the application of IFR positive effect on the frequency of stock trading can be concluded that the first hypothesis is accepted.

To pengungkapan_informasi have a significance value of 0.002, meaning that the disclosure of information on the company website has a positive effect on the frequency of stock trading. This means that the second hypothesis is accepted.

Discussion of the First Hypothesis

Based on testing of the influence of Internet Financial Reporting (Praktik_IFR) against the frequency of trading in shares (frekuensi_saham) can be seen that the variable has a positive effect on frekuensi_saham praktik_IFR. 328.114 praktik_IFR variable coefficients are of 0.003 and sig. Value sig. (0.003) $\alpha (0.05)$, this means praktik_IFR variables significant at the 5% level.

Positive influence is in line with that expressed by Ball and Brawn (1968) and Fama et al., (1969) that the stock will move when the information is useful to enter the market. Any disclosure of information would make the investor to re-examine their assessment of the value of stock and made the decision to sell or hold shares.

Discussion of the Second Hypothesis

From the results of statistical tests can be seen that there is a positive relationship between the level of disclosure in the company's website (pengungkapan_informasi) with shares trading frequency (frekuensi_saham). Variable levels of disclosure in the company's website (pengungkapan_informasi) has



a coefficient of 0.002 311 562 and sig. Value sig. (0.002) $< \alpha \alpha$ (0.05), this means that the variable level of disclosure of significant information on the company website at level 5%.

Positive effect is consistent with the disclosed and Zuhrotun Sari (2006) is one way to reduce the information asymmetry is to provide a signal to the external form of reliable financial information and will reduce the uncertainty about the future prospects of the company. Lai et al., (2010) also expressed a great benefit for companies to disclose as much information as possible so that investors are able to distinguish between good companies and bad ones.

CONCLUSIONS AND RECOMMENDATIONS

Conclusion

The conclusions that can be drawn from this study are as follows:

1. Internet Financial Reporting has positive effect on the frequency of stock trading on trading, services, and investment company.
2. Degree of Information disclosure on company's website has positive effect on the frequency of stock trading on trading, services, and investment company.

Research Limitations

This study has several limitations that require improvement and development in subsequent studies. The limitation of this study are as follows:

1. Observation period is limited for 3 years, the years 2009-2011 making it less able to predict for long-term results.
2. Researchers can only take two independent variables, namely Internet Financial Reporting (IFR) and the level of disclosure in the company's website.

Suggestion

1. Observation period should be extended in order to better predict for long-term results.
2. For further research are expected to be able to add other variables related to stock trading so that the expected frequency of research results obtained could be more comprehensive.
3. Further research in order to involve other researchers to conduct a reassessment to crosscheck.

REFERENCES

- Almilia, Luciana Spica. , 2009. "Analysis of Financial And Quality Content On Sustainability Reporting Company Website Go Public In Indonesia". Papers presented in National Seminar on Application of Information Technology 2009 (SNATI 2009), London, 20 June 2009.
- Ashbaugh, H; K. Johnstone; and T. Warfield. Of 1999. Corporate Reporting on the Internet. Accounting Horizons, Vol 13 No.3, pp 241-257.
- Ball, R & P. Brown. Of 1968. An Empirical Evaluation of Accounting Income Numbers. Journal of Accounting Research (Autumn), Vol 6, No.2, pp. 159-178.
- Budisusetyo, Saso & Luciana Spica Almilia. , 2007. "Corporate Internet Reporting of Banking Industry



- and LQ45 Firms: An Indonesian Example". Papers published in Proceedings of the 1st Parahyangan International Accounting & Business Conference 2008, London, 13-15 June 2008.
- Cooper, Donald R. & C. William Emory. , 2004. Business Research Methods. New York: grants.
- Chandra, Princess Aulia. , 2008. "Factors Affecting Financial Reporting Inclusion of company's website (Internet Financial Reporting)". Faculty of Economics, University of Diponegoro.
- Chariri, Anis&Hanny Sri Lestari. , 2005. "Analysis of Factors Affecting Financial Reporting on the Internet (Internet Financial Reporting) in the Company's Website".Faculty of Economics, University of Diponegoro.
- Easley, E. & M. O'Hara. , 2004. Information and the Cost of Capital. Journal of Finance, 59, 1553-1584.
- Fama, E. F; L. Fisher; M. C. Jensen; and R. Roll.1969. The Adjustment of Stock Prices to New Information. International Economic Review, Vol 10 No.1, pp 1-21.
- Ghozali, Imam. , 2006. Application of Multivariate Analysis with SPSS program. London: BP-UNDIP.
- Hargyantoro, Hidalgo. Of 2010. Effect of Internet Financial Reporting and Disclosure Levels Website Against Frequency Share Trading Company. Thesis published. London: Faculty of Economics, University of Diponegoro.
- Internet World Stats.N.d. "World Internet Usage and Populations Statistics". ([Http://www.internetworldstats.com/stats](http://www.internetworldstats.com/stats). Accessed on 2 November 2011).
- Internet World Stats.N.d. "Internet Usage and Populations Statistics in Asia". ([Http://www.internetworldstats.com/stats](http://www.internetworldstats.com/stats). Accessed on 2 November 2011).
- No decision of the Chairman. Kep-38/PM/1996 dated January 17, 1996.
- Khan, Tehmina. , 2006. "Financial Disclosure Reporting On The Internet: An International Perspective". Faculty of Business and Law School of Accounting, Victoria University, Australia.
- Kusumawadini, Arum. Of 2011. Analysis of Factors Affecting Financial Reporting Through the Internet (Internet Financial reporting) in the Company's Website. Thesis published. London: Faculty of Economics, University of Diponegoro.
- Lai, Syou-Ching; Cecilia Lin; Hung-Chih Li; and Frederick H. Wu.Of 2010.An Empirical Study of the Impact of Internet Financial Reporting on Stock Prices. The International Journal of Digital Accounting Research, Vol 10, pp 1-26.
- Marston, Claire. , 2003. Financial Reporting on the Internet by Leading Japanese Companies. Corporate Communications: An International Journal, Vol 8 No.1, pp 23-24.
- Pervan, Ivica. , 2006. Voluntary Financial Reporting on the Internet-Analysis of the Practice of Croatian and Slovene Joint Stock Companies Listed. Financial Theory and Practice, Vol 30 No.1, pp 1-27.
- Samsul, Mohammad. , 2006. Capital Markets and Portfolio Management. New York: grants.
- Sari, Ratna Chandra &Zuhrotun. , 2006. Keinformatifan Profit on Stock And Bond Markets: Liquidation Option Hypothesis Testing. National Symposium on Accounting 9, Padang.
- Financial Accounting Standards # 1 in 2009.
- Stice, James D; Earl K. Stice, and K. F. Skousen. , 2009. Financial Accounting. New York: Four Salemba.
- Supriadi, DeriAlambudiarti. Of 2010. Effect of Company Characteristics Of Completeness of Financial Statements in the Registered Automotive Company in Indonesia Stock Exchange. London: University of National Development.
- Warren, Carl S; James M. Reeve; Philip E. Fess. , 2008. Introduction to Accounting. New York: Four Salemba.

Combined Effect of Executive Stock Option Granting and Blockholder Ownership on Firm Performance in Malaysia

AHMAD IBN IBRAHIMY*
 Bachelor of Accounting Program
 Universiti Malaysia Terengganu
 21030 Kuala Terengganu, Terengganu
 MALAYSIA
 ibrahimy@umt.edu.my

RUBI AHMAD
 Department of Finance and Banking
 University of Malaya
 50603 Kuala Lumpur
 MALAYSIA
 rubi@um.edu.my

Abstract

The problem of providing incentives and large shareholders' impact on firm performance has been well established in the literature. Unlike US, the key agency problem encountered by Malaysian firms is the conflicts of interests between majority and minority shareholders. Using fixed effect panel data analysis, this study examines the combined effects of Executive Stock Option (ESO) granting and blockholder ownership as governance mechanisms on performance of Malaysian non-financial public listed companies. Despite the consistent significant relationship with increasing rate of beta coefficients, the results exhibit weaker effects on firm performance by both market and accounting based measurements. The significant results suggest that ESO granting is increasing the firm value couple with little influence of blockholders ownership by monitoring the executives of the firms. Overall, the findings indicate that ESO granting and blockholder ownership enhance the performance as corporate governance mechanisms to alleviate the agency costs by aligning / monitoring the interests between executives and shareholders which support convergence of interests and efficient monitoring hypotheses. However, relatively weaker effects of blockholder ownership may due to hidden intention of blockholders of satisfying their own interests rather than maximizing shareholders' wealth.

Key Words: ESO Granting, Blockholders, Agency Problem, Firm Performance, Malaysia



INTRODUCTION

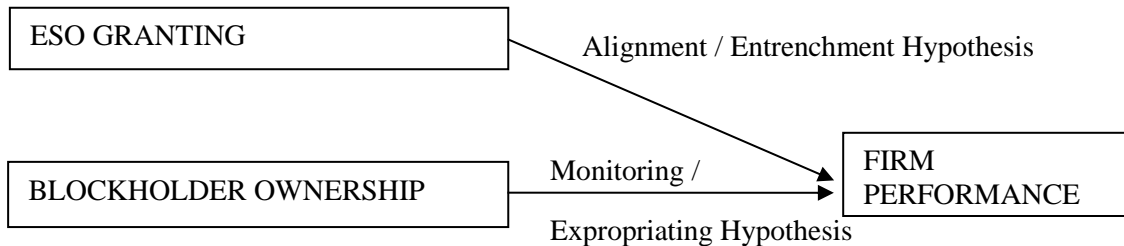
The problem of providing incentives and large shareholders' impact on firm performance has been well established in the literature for managers to make decisions that maximize shareholders wealth. However, there are very few empirical evidences of corporate governance mechanisms based on South East Asian countries. The key agency problem encountered by Malaysian firms is the conflicts of interests between majority and minority shareholders. In Malaysia, two-thirds firms are controlled by a single shareholder with high ownership concentration and limited conflicts between large shareholders and managers (Claessens et al. 2000) has a different set of agency problems all together. These corporate scenarios of Malaysian firms differ from the developed markets' dispersed ownership structure where introduction of Executive Stock Option Scheme (ESOs) is a burning question of aligning the interests between executives and the shareholders. Consequently, when large shareholders are the board members, decisions carried out by them are a question of whether it would incline to benefit them at the cost of minority shareholders. This refers to the issue of conflicts between majority and minority shareholders in Asian countries. Therefore, high concentrated ownership, presence of weak corporate governance in Asian countries (Zhuang, 2001); and the limited minority rights are the motivations of this study that allow us to test the effectiveness of governance mechanisms on firm performance.

The main component is 'contract' leading the relationship between principal and agent (Eisenhardt, 1989) in Corporation. For this reason, theory focuses on determining the efficient contract with assumptions about people, organizations and information. Whether behavior-oriented or outcome-oriented contract is more efficient becomes an issue. Examples of behavior-oriented contract capture salaries, hierarchical governance and outcome-oriented contract include commissions, stock options, market governance etc. Jensen and Meckling (1976) define the agency problems as a contract when the principal(s) hire the agent(s) to carry out their works that involve decision making right. If both parties are focused on their own interests to maximize satisfaction, there will be a conflict between them. As such, agents will not work for the best interests of principal always. The principal can reduce this dispersion of different attitudes by designing incentive plans and also by limiting agent's unusual activities that involve monitoring costs. The incentive as a dollar amount is decreasing the principal's wealth named as "residual loss." The relationship between principal and agent fits well with good relationship between owners and managers in a corporation.

Two techniques of alleviating of agency problem are monitoring (Eaton & Rosen, 1983; Lewellen, Loderer, & Martin, 1987) and incentives (Bizjak, Brickley, & Coles, 1993; Jensen & Murphy, 1990b). Jensen and Murphy (1990a) emphasize that stock based compensation gives more incentives to the executives rather than cash based incentives to maximize the shareholders wealth. But there are few evidences whether insider versus outsider ownership or the composition of board of directors influences the executive compensation policy. By focusing on compensation structure rather than the level of compensation Jensen and Murphy (1990a) found that, (a) with more outside directors, there is higher stock based compensation (b) inverse relation between stock based compensation and stock holdings, and (c) large outside blockholder firms use less stock based compensation. They also found positive relation with stock based executive compensation and executive stock holding with firm performance. Generally it is assumed that stock based compensation is more popular when agency costs are high and monitoring is difficult. The convergence / entrenchment hypotheses conceive that at low level of managerial ownership firm value will increase due to market discipline that align the interests between managers and outside shareholders (Jensen & Meckling, 1976). As managerial stake increases they may become entrenched and the firm value start to decline. Large shareholders also may expropriate minority shareholders' wealth as they are holding a large block of shares. The main objective of this study, therefore, is to examine the combined effects of Executive Stock Option



(ESO) granting and blockholder ownership as governance mechanisms that affect firm value. The relationship between ESO granting and blockholder ownership is depicted below:



LITERATURE REVIEW

With the emergence and acceptance of agency theory, the concern on executive compensation becomes popular among academicians after “Management Compensation and Managerial Labor Market” conference that was held at University of Rochester in 1984. Based on the value implications of stock option grants, Lam and Chng (2006) examined the relation between the executive stock option (XSO) grants and the firm performance using instrumental variables. By controlling for firm and industry level heterogeneity, they found a positive relationship of executive stock option grants to firm performance which is consistent with value enhancement notion that increasing firm value and reducing the agency costs. Hillegeist and Penalva (2003) also found consistent evidence by analyzing the performance consequences of employee stock options for US firms. On the other hand, Oyer and Schaefer (2005) gathered US data from three sources of ESO grants and conduct a cross-sectional study on middle managers. They reject an incentive based justification for broad based incentive plans. Yermack (1995) studied stock option awards to CEOs of large US corporations based on the comprehensive agency and financial contracting theory. Using a Black-Scholes approach, study found weak support for optimal compensation practices or the theories of optimal compensation contract is incomplete that reduce agency costs.

Lins (2003) used 1433 firms from 18 emerging markets to investigate whether management stock ownership and outside blockholder ownership affect firm value. In low protected shareholders countries, the study found a positive relation between blockholders and firm value. In addition, firm value is low when voting rights exceeds the cash flow rights in these countries. On the other hand, Slovin and Sushka (1993) explored how ownership concentration affect firm performance and control of US firms by examining obituary notices published in the Wall Street Journal. On the effects of death of inside blockholders, their findings reveal the negative relation of shareholder’s wealth increases and ownership concentration decreases with extensive corporate control develops. In other words, they found the positive relation between stock price and the death of inside blockholders. Cronqvist and Nilsson (2003) estimated the agency costs of controlling minority shareholders using a panel data of Swedish firms. The evidence showed a negative relation between firm performance and different categories of controlling shareholders ranging the agency costs of 6% to 25%.

There are only two studies that look into ESOs effect on firm performance in Malaysian based literatures. Bacha et al. (2009) examined several issues related to the implementation of ESOs among Malaysian firms based on ESOs firms and their industry peers. They found that ESOs adopted firms have marginally higher mean returns and lower volatility compare to their pre-ESO peers but statistically insignificant. Large firms are more likely to initiate ESOs



when the market value of their stock is low; and the market reaction to ESO announcement is significantly negative which is similar to Blasi et al. (1996) findings of weakened performance for ESO firms. Another study by Ghazali and Taib (2011) used logistic regression to observe the impact of ESOs adoption, rather than ESOs granting, on firm performance. They found a very weak impact of ESOs adoption on firm's performance using the observations from 1989 to 2004. In 2004, Security Commission (SC), Malaysia approved the ESOs by-law of governing. Unlike US studies of ESOs adoption, they did not find any significant differences between ESOs adopted and non-adopted firms' performance. Our study considers ESO granting and blockholder ownership as corporate governance mechanisms to tackle agency problem, and therefore increasing firm value. Khatri et al. (2002), Claessens et al. (2000) and Lim (1981) studied the ownership structure effect to firm performance and found the blockholders having a significant impact on performance in Malaysia. They also found that coupled with the influence on business operations, most blockholders are having a seat (or proxy) in Board of Directors. On the other hand, Ngui and Voon (2008) examined the relationship between outside blockholders and firm performance of Malaysian firms using a single structural model and found a negative relationship. Two types of ownership concentration are applied in the study, insider ownership and outside blockholders. Blockholders' negative effect on firm performance indicates that expectation of blockholders alleviate the managerial (insiders) entrenchment. According to Yeo et al. (2002), existence of major blockholders can be an effective monitoring mechanism on managerial incentives when there is a low level of managerial ownership.

RESEARCH METHODOLOGY

The models are developed to identify how combination of ESO granting and blockholders may have influence the firm performance in Malaysia after controlling firm specific variables. Panel data fixed effect model is used to observe the relations as it is more appropriate to capture the heterogeneity of ESO grants (Lam & Chng, 2006; Zhou, 2001). The study also employed pooled effect model to ensure the best fitted model that satisfies the assumptions of Classical Linear Regression Model (CLRM). The period of study covers from 2002 until 2008. Data are collected purposive sampling basis and eligibility requirement of a company to enter into sample is: presence of ESOs adoption for the entire period. Altogether, the sample is comprised of 205 companies out of 299 companies that adopted ESOs during the period. Rest of them is non-adopting ESOs companies. It is important to ensure that all companies are active during the study period and should not be classified as PN4 companies. Finally, 4 of the 205 companies are excluded due to incomplete data that are inactive. Therefore, the final sample consists of 201 non-financial companies of Bursa Malaysia from all sectors except financial industry. Data for ESOs adoption, granting and blockholder ownership were detected through Bursa Malaysia web information, Annual Reports' of respective companies. The empirical relationships for firm i in the year t are given below:

$$TQ_{it} = \alpha + \sum \beta_1 ESO_{it} + \beta_2 BL_{it} + \beta_3 RV_{it} + \beta_4 PV_{it} + \beta_5 DR_{it} + \beta_6 G_{it} + \beta_7 S_{it} + u_{it} \quad (1)$$

$$ROE_{it} = \alpha + \sum \beta_1 ESO_{it} + \beta_2 BL_{it} + \beta_3 RV_{it} + \beta_4 PV_{it} + \beta_5 DR_{it} + \beta_6 G_{it} + \beta_7 S_{it} + u_{it} \quad (2)$$

Where, TQ = Tobin's Q; ROE = Return on Equity; ESO = ESO Granting (2002, 2003, 2004, 2005, 2006, 2007); BL = Blockholder Ownership; RV = Return Volatility; PV = Profit Volatility; DR = Debt Ratio; G = Growth of the Company; S = Size of the Company.



Table 1: Summary of Dependent Variables

Variable	Variable Name	Definition
TQ	Tobin's Q	A ratio of the market value of a company to the replacement costs of the company's assets (Villalonga and Amit, 2006; Anderson and Reeb, 2003)
ROE	Return on Equity	A ratio of the net income divided by the shareholders' equity (Duffhues et al. 2002; Pedersen and Thomsen, 1999)

Table 2: Summary of Independent Variables

Variable	Variable Name	Definition
ESO	ESO Granting	Dummy variable taking a value of 1 if company grant ESO for a particular year, otherwise 0 (2002, 2003, 2004, 2005, 2006, 2007) (Blasi et al. 1996; Conte et al. 1996)
BL	Blockholder Ownership	Blockholders as shareholders who own 5% of shares and above, otherwise 1 (McConnell et al. 2008; Bhabra, 2007)
RV	Return Volatility	Standard deviation of yearly stock return, one year lag (Ittner et al. 2003; Mehran and Tracy, 2001)
PV	Profit Volatility	Standard deviation of return on equity yearly basis (Pedersen and Thomsen, 1999; Prowse, 1992)
DR	Debt Ratio	Leverage, measured as total debt divided by book value of total assets multiply 100 (Wei & Zhang, 2008; Wiwattanakantang, 2001)
G	Growth	Growth of the company, measured as five years average of sales growth (La Porta et al. 2002; Jensen, Solberg, & Zorn, 1992)
S	Size	Size of the company, measured as natural log of total assets (Kaserer & Moldenhauer, 2008; Kim et al. 2007)

Before running the models, Hausman test is performed. One way of model selection to fit the data properly could be done using Hausman's specification test (Dougherty, 2006). According to Baltagi (2005), if the assumption of random effect model of there is no correlation between independent variables and the error term is not fulfilled, the coefficients estimated by the random effect model will be biased and inconsistent. In order to specify the best model Hausman's specification test is performed to test the null hypothesis of there is no difference between fixed effect model and the random effect model or



whether the correlation between independent variables and the error term is zero. As Chi-square test statistics are significant for all models, we reject the null hypotheses. The results are indicating that there is no difference between fixed effect and random effect model. In other words, there is no correlation between error terms and the explanatory variables. Therefore, fixed effect model is employed as the fixed effect estimator of the coefficients is considered unbiased and consistent.

EMPIRICAL RESULTS

Table 3 demonstrates the results of both pooled and fixed effect OLS and GLS regression estimations to test the effects of respective hypotheses on firm performance (TQ). Results of two estimators are reported in order to compare the estimations. ESO granted in year 2003 and year 2006 are positively significant by both estimators. Regression results show that stock option granted in 2002 has positive significant effect on the performance (TQ) in 2003, and so on. Year 2007 again not significant may be due to the economic slowdown in Malaysia that begins in the 3rd quarter of this year. The increasing rates of the coefficients suggest that ESO granting tying the executives more closely to firm performance that eventually supporting convergence of interests / incentive alignment hypothesis. The finding is similar with Lam and Chng (2006) but contrasts with Oyer and Schaefer (2005); Yermack (1995). On the other hand, blockholders is positively correlated with firm performance. The insignificant positive relation of blockholders is referring their effects to performance with limited influence.

Table 3: Pooled and Fixed Panel: Combined Effects with Industries

Against TQ Variables	OLS		GLS	
	Pooled	Fixed	Pooled	Fixed
Intercept ©	1.14***	0.87**	1.22***	0.94***
ESO Granted (2002)	0.04	0.04	0.04	0.04
ESO Granted (2003)	0.19***	0.07	0.19***	0.08
ESO Granted (2004)	0.07	0.02	0.07	0.02
ESO Granted (2005)	-0.004	0.03	-0.003	0.03
ESO Granted (2006)	0.25**	0.24*	0.25**	0.24*
ESO Granted (2007)	0.19	0.17	0.19	0.16
Blockholders (BL)	0.0007	0.0007	0.0005	0.0005
Return Volatility (RV)	-0.27	-0.11	-0.30	-0.14
Profit Volatility (PV)	0.04***	0.04***	0.04***	0.04***
Debt Ratio (DR)	-0.005***	-0.005***	-0.005***	-0.005***
Growth (G)	0.002***	0.002***	0.002**	0.002**



Size (S)	0.03*	0.03**	0.02*	0.03**
R²	0.29	0.30	0.29	0.30
Adjusted R ²	0.28	0.29	0.28	0.28
F-statistic	28.61***	22.72***	27.88***	22.41***
D-W statistic	0.76	0.74	0.70	0.68
Hausman's Specification Test: Chi-square static: 121.90***				

*** 1% Significant level ** 5% Significant level * 10% Significant level

Table 4 exhibits the results of both pooled and fixed effect OLS and GLS regression estimations to test the effects of respective hypotheses on firm performance (ROE). The result reports similar evidences where ESOs granted in year 2004, year 2006 and year 2007 are significant against firm performance. This positive effect of ESO granted result is consistent with Duffhues et al. (2002) finding. For both OLS and GLS estimations, blockholder ownership is positively related with firm performance where it is significant for pooled and fixed effect GLS estimator. Overall, this positive relationship is indicating a modest influence of blockholder ownership on firm performance of ESOs adopted firms.

Table 4: Pooled and Fixed Panel: Combined Effects with Industries

Against ROE Variables	OLS		GLS	
	Pooled	Fixed	Pooled	Fixed
Intercept ©	-45.64***	-41.29***	-40.35***	-36.12***
ESO Granted (2002)	1.60	2.45	1.66	2.55
ESO Granted (2003)	0.88	2.59	1.07	2.79
ESO Granted (2004)	3.30**	2.70	3.42**	2.79
ESO Granted (2005)	3.10	4.09	3.37	4.33*
ESO Granted (2006)	3.11*	3.90*	3.28*	3.87*
ESO Granted (2007)	11.14**	8.92*	11.66**	9.20*
Blockholders (BL)	0.03	0.03	0.03*	0.03*
Return Volatility (RV)	-21.63***	-22.67**	-23.37***	-24.38***
Profit Volatility (PV)	-0.54	-0.54	-0.63*	-0.64*
Debt Ratio (DR)	-0.20***	-0.20***	-0.19***	-0.19***



Growth (G)	0.11***	0.10***	0.10***	0.10***
Size (S)	2.87***	2.78***	2.64***	2.56***
R²	0.22	0.22	0.22	0.22
Adjusted R ²	0.21	0.21	0.21	0.21
F-statistic	19.19***	15.05***	19.42***	15.22***
D-W statistic	1.25	1.24	1.19	1.19
Hausman's Specification Test: Chi-square static: 34.72***				

*** 1% Significant level

** 5% Significant level * 10% Significant level

Among control variables, return volatility is negatively significant with high magnitude of beta coefficients. Profit volatility is found to have negative relationship with firm performance and significant with GLS estimators. Debt ratio and growth are statistically significant at 1% level by both estimators where leverage (debt ratio) is inversely related with firm performance. Negative relationship of debt ratio implies that larger the leverage smaller the pay-performance ratio of top management compensation. The increased magnitude of the coefficients of these variables is indicating the financial importance of Malaysian economy. Firm's size is positively significant with firm performance at 1% level by both estimators. In terms of goodness of fit of the models, both OLS and GLS estimators have same explanatory power (R^2).

CONCLUSION

The objective of this study is to determine the combined effects of Executing Stock Option (ESO) granting and blockholder ownership on firm performance as corporate governance mechanisms. The combined effects of ESO granting and blockholder ownership are tested. Despite the consistent significant relationship with increasing rate of beta coefficients, the results exhibit weaker effects on firm performance by both measurements. Although, the significant results suggest that ESO granting is increasing the firm value couple with little influence of blockholders ownership by monitoring the executives. Notably, there are economic sharp contraction in year 2005 and 2007 in Malaysian economy. Overall, the findings indicate that ESO granting and blockholder ownership enhance the performance as corporate governance mechanisms to alleviate the agency costs by aligning / monitoring the interests between executives and shareholders. Nonetheless, relatively weaker effects when blockholders is incorporated in the model may due to hidden intention of blockholders of satisfying their own interests rather than maximizing shareholders' wealth. In the presence of poor corporate governance structure, there may have less fruits of ESOs adoption where blockholders may take the opportunity to benefit them when option is in the money. This interference bring the doubt of ESO granting in Malaysia whether it is for intended reason of aligning interests between executives and shareholders to maximize shareholders' wealth or one way of expropriating corporate wealth by granting ESO at discount price. But, there is no evidence of expropriating minority shareholders' wealth by blockholders. We found a modest influential effect of blockholder ownership on firm performance as a monitoring mechanism in the scenario where blockholders are also in the management.



References:

- Anderson, R. C., & Reeb, D. M. (2003). Founding-family ownership and firm performance: Evidence from the S&P 500. *Journal of Finance*, 1301-1328.
- Bacha, O. I., Zain, S., Rasid, M., & Mohamad, A. (2009). GRANTING EMPLOYEE STOCK OPTIONS (ESOs), MARKET REACTION AND FINANCIAL PERFORMANCE. *Asian Academy of Management Journal of Accounting and Finance*, 5(1), 117-138.
- Baltagi, B. H. (2005). *Econometric analysis of panel data*: Wiley.
- Bhabra, G. S. (2007). Insider ownership and firm value in New Zealand. *Journal of Multinational Financial Management*, 17(2), 142-154.
- Bizjak, J. M., Brickley, J. A., & Coles, J. L. (1993). Stock-based incentive compensation and investment behavior. *Journal of Accounting and Economics*, 16(1-3), 349-372.
- Blasi, J. B., Conte, M., & Kruse, D. (1996). Employee stock ownership and corporate performance among public companies. *Indus. & Lab. Rel. Rev.*, 50, 60.
- Claessens, S., Djankov, S., & Lang, L. H. P. (2000). The separation of ownership and control in East Asian Corporations. *Journal of Financial Economics*, 58(1-2), 81-112.
- Conte, M. A., Blasi, J., Kruse, D., & Jampani, R. (1996). Financial returns of public ESOP companies: Investor effects vs. manager effects. *Financial Analysts Journal*, 51-61.
- Cronqvist, H., & Nilsson, M. (2003). Agency costs of controlling minority shareholders. *Journal of Financial and Quantitative Analysis*, 38(04), 695-719.
- Dougherty, C. (2006). *Introduction to Econometrics*: Oxford University Press.
- Duffhues, P., Kabir, R., Mertens, G., & Roosenboom, P. (2002). Employee stock option grants and firm performance in the Netherlands. *Open Access publications from Tilburg University*.
- Eaton, J., & Rosen, H. S. (1983). Agency, Delayed Compensation, and the Structure of Executive Remuneration. *Journal of Finance*, 38(5), 1489-1505.
- Eisenhardt, K. M. (1989). Agency theory: An assessment and review. *Academy of Management Review*, 57-74.
- Ghazali, Z., & Taib, F. M. (2011). *An Effective Interests Alignment Mechanism or a Tool to Expropriate: A Review of Malaysian ESOS Adoption*. Paper presented at the Asia-Pacific Business Research Conference, KL, Malaysia.
- Hillegeist, S. A., & Penalva, F. (2003). Stock option incentives and firm performance. *Social Science Research Network Working Paper Series*.
- Ittner, C. D., Lambert, R. A., & Larcker, D. F. (2003). The structure and performance consequences of equity grants to employees of new economy firms. *Journal of Accounting and Economics*, 34(1-3), 89-127.
- Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics*, 3(4), 305-360.



- Jensen, M., & Murphy, K. (1990a). CEO incentives: it's not how much you pay, but how. *Michael C. Jensen, FOUNDATIONS OF ORGANIZATIONAL STRATEGY, Harvard University Press, 1998; Harvard Business Review, No. 3, May-June 1990.*
- Jensen, M. C., & Murphy, K. J. (1990b). Performance pay and top-management incentives. *Journal of political economy, 225-264.*
- Jensen, G. R., Solberg, D. P., & Zorn, T. S. (1992). Simultaneous determination of insider ownership, debt, and dividend policies. *Journal of Financial and Quantitative Analysis, 27(2), 247-263.*
- Kaserer, C., & Moldenhauer, B. (2008). Insider ownership and corporate performance: evidence from Germany. *Review of Managerial Science, 2(1), 1-35.*
- Kim, K. A., Kitsabunnarat-Chatjuthamard, P., & Nofsinger, J. R. (2007). Large Shareholders, Board Independence, and Minority Shareholder Rights: Evidence from Europe. *Journal of Corporate Finance, 13(5), 859-880.*
- Khatri, Y., Leruth, L., & Piesse, J. (2002). *Corporate performance and governance in Malaysia: International Monetary Fund.*
- La Porta, R., Lopez, F., Shleifer, A., & Vishny, R. (2002). Investor Protection and Corporate Valuation. *Journal of Finance, 57(3), 1147-1170.*
- Lam, S. S., & Chng, B. F. (2006). Do executive stock option grants have value implications for firm performance? *Review of Quantitative Finance and Accounting, 26(3), 249-274.*
- Lewellen, W., Loderer, C., & Martin, K. (1987). Executive compensation and executive incentive problems: An empirical analysis. *Journal of Accounting and Economics, 9(3), 287-310.*
- Lim, M. H. (1981). *Ownership and control of the one hundred largest corporations in Malaysia: Oxford University Press Kuala Lumpur.*
- Lins, K. V. (2003). Equity ownership and firm value in emerging markets. *Journal of Financial and Quantitative Analysis, 38(1), 159-184.*
- McConnell, J. J., Servaes, H., & Lins, K. V. (2008). Changes in insider ownership and changes in the market value of the firm. *Journal of Corporate Finance, 14(2), 92-106.*
- Mehran, H., & Tracy, J. (2001). The Effect of Employee Stock Options on the Evolution of Compensation in the 1990s. *Economic Policy Review, 7(3), 17-34.*
- Ngui, K. S., & Voon, M. L. (2008). Ownership concentration and performance of Malaysian listed firms. Retrieved from <http://ssrn.com/abstract=1101222>
- Oyer, P., & Schaefer, S. (2005). Why do some firms give stock options to all employees?: An empirical examination of alternative theories. *Journal of Financial Economics, 76(1), 99-133.*
- Pedersen, T., & Thomsen, S. (1999). Economic and systemic explanations of ownership concentration among Europe's largest companies. *International Journal of the Economics of Business, 6(3), 367-381.*
- Prowse, S. D. (1992). The structure of corporate ownership in Japan. *Journal of Finance, 1121-1140.*



- Slovin, M. B., & Sushka, M. E. (1993). Ownership concentration, corporate control activity, and firm value: Evidence from the death of inside blockholders. *Journal of Finance*, 1293-1321.
- Villalonga, B., & Amit, R. (2006). How do family ownership, control and management affect firm value? *Journal of Financial Economics*, 80(2), 385-417.
- Wei, K., & Zhang, Y. (2008). Ownership structure, cash flow, and capital investment: Evidence from East Asian economies before the financial crisis. *Journal of Corporate Finance*, 14(2), 118-132.
- Wiwattanakantang, Y. (2001). Controlling shareholders and corporate value: Evidence from Thailand. *Pacific-Basin Finance Journal*, 9(4), 323-362.
- Yeo, G. H. H., Tan, P. M. S., Ho, K. W., & Chen, S. S. (2002). Corporate ownership structure and the informativeness of earnings. *Journal of Business Finance & Accounting*, 29(7 & 8), 1023-1046.
- Yermack, D. (1995). Do corporations award CEO stock options effectively? *Journal of Financial Economics*, 39(2-3), 237-269.
- Zhou, X. (2001). Understanding the determinants of managerial ownership and the link between ownership and performance: comment. *Journal of Financial Economics*, 62(3), 559-571.
- Zhuang, J. (2001). *Corporate governance and finance in East Asia: a study of Indonesia, Republic of Korea, Malaysia, Philippines, and Thailand* (Vol. 2): Asian Development Bank.

School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA

Faculty of Business and Accountancy
University of Malaya
50603 Kuala Lumpur
MALAYSIA



The Role and Influence of Corporate Leader Values on Corporate Governance Mechanisms and Financial Reporting Quality

WAN ZANANI WAN ABDULLAH
 Department of Basic Knowledge
 Centre of Fundamental and Liberal Education
 Universiti Malaysia Terengganu
 21030 Kuala Terengganu, Terengganu
 MALAYSIA
 zanani@umt.edu.my

PROF DR FAUZIAH MD TAIB
 School of Management
 Universiti Sains Malaysia
 11800 USM, Pulau Pinang
 MALAYSIA
 mfauziah@usm.my

DR AMIRUL SHAH MD SHAHBUDIN
 School of Management
 Universiti Sains Malaysia
 11800 USM, Pulau Pinang
 MALAYSIA
 amirulshah@usm.my

Abstract

Even after twenty years of implementing corporate governance system, corporate scandals and failures are still happening. Most empirical studies show inconsistent and at best, inconclusive findings regarding the effects of corporate governance mechanisms (board independence and size, CEO duality, audit committee independence and expertise, ownership structure) on quality of financial reporting. The current corporate governance systems only concentrate on improving the structure in enhancing quality of corporate governance mechanisms but ignore quality of corporate people. Thus, it is important to study the role of corporate leader values as an organization is typically shaped up by the attitude, values and vision of a corporate leader. Previous doctrine separating the organization and the owner is no longer tenable as it tends to widen the gap between functions of ownership and management (CEO). Thus, this study will fill the void by examining the role and influence of corporate leader's values on corporate governance mechanisms and earnings management. Reporting quality of 120 non-financial companies listed on Bursa Malaysia is examined for the year 2009 and 2010. The study employs modified Jones (1991) model to measure earnings management through calculation of discretionary accruals (DA) while the role and influence of corporate leader values are measured through workplace spirituality approach as proposed by Ashmos and Duchon (2000). The self-evaluated questionnaire has been distributed to corporate leaders, specifically CEOs, to determine the perceived of corporate leader values in each company. The findings of the study show that the corporate leader values moderates the relationship between corporate governance mechanisms and earnings management. Sense of spiritual health (vertical relationship with Creator) and sense of recognition and appreciation (horizontal relationship with humans) are two crucial values of corporate leader that can strengthen and support the corporate governance mechanisms to be effective in mitigating earnings management especially board



independence, audit committee expertise and insider ownership. These findings suggest that the integration of corporate leader values in corporate governance system is important to enhance the effectiveness of corporate governance mechanisms and improve quality financial reporting. The study found that value based governance is the best internal solution to corporate governance system and it becomes a supplemented approach to corporate governance mechanisms that as an external solution. Therefore, the human governance concept which is underlies by spiritual leadership theory, workplace spirituality and stewardship theory is crucial to be implemented by corporations in building a strong corporate governance system in mitigating earnings management.

Key Words: corporate governance mechanisms, corporate leader values, earnings management, financial reporting quality

1. INTRODUCTION

The importance of good corporate governance became a debate among researchers, academicians, regulators, practitioners, policy makers and even society after the biggest economic crisis occurred around the world in the late 1990s. The consequences of corporate failure will affect the companies, the capital market, the economic stability, social development and the well-being of shareholders and stakeholders. In the early 2000s, the biggest corporation in the United States, Enron Corporation collapsed, followed by the failure of WorldCom, HIH, OneTel, Pramalat and other big companies. Following these corporate scandals, the United States of America government approved the Sarbanes-Oxley Act in July 2002. However, corporate failures are still occurring as shown by the recent corporate collapses of Northern Rock, Bear Stearns and Bernard L. Madoff Investment Securities in 2009. This scenario of corporate scandals also occurred in Malaysia before and after the Malaysian Code of Corporate Governance (MCCG) is revised in 2007. The examples of the companies are Transmile Group Bhd, Megan Media, NasionCom Berhad, United U-Li Corporation Berhad and OCI Berhad in 2007 and Oilcorp Bhd in 2008. Most of responsible person involved in corporate failures are top corporate leaders, especially Chief Executive Officers (CEOs), Chief Financial Officers (CFOs) and corporate directors. Experiences of corporate scandals and failures revealed that company management, especially top management, acted not for the best interest of their shareholders (Staubus, 2005). They tended to manipulate earnings reports to show good company performance in order to get better compensation or cash bonuses (Baker *et al.*, 2000; Efendi *et al.*, 2007).

At present, there are many studies that look into the effectiveness of various corporate governance mechanisms in influencing companies' quality of financial reporting (Davidson *et al.*, 2005; Hutchinson *et al.*, 2008; Jaggi *et al.*, 2009; Lin and Hwang, 2010; Hadani *et al.*, 2011). Using the agency theory these studies hypothesise that the financial reporting quality will be improved upon putting these internal and external corporate governance mechanisms in place. Even though there are evidence to indicate that both the internal (board independence, board size, audit committee independence, audit committee expertise, CEO duality, insider ownership and outsider ownership) and external (institutional shareholdings) are effective mechanisms, accounting scandals, and frauds continue to happen. Indirectly the evidence suggests that the rule-based governance (both internal and external mechanisms) is not working to bring about the intended outcomes especially financial reporting quality. Even some of the earlier evidences are not consistent and contradictory (Norman *et al.*, 2005; Abdul Rahman and Mohamed Ali, 2006; Abdullah, 2006; Siregar and Utama, 2008; Ghosh *et al.*, 2010). This points out to the possibility of having another factor at work that could explain the situation better.

According to Arfah and Aziuddin (2008), the current practices of corporate governance are not able to bring the desired behavioural conduct among the trustees of public interest. Mehra (2005) claimed that current corporate governance practices are imposed with legislation alone that is concerned only on a ticking boxes approach while the substance of the law is ignored. He stressed that issues of corporate governance actually are issues of hearts.



Thus, it requires the solutions that are based on hearts (Taib, 2009). Adam (2003) argued that the root cause of corporate governance failure is not the rule itself but behaviour of corporate leaders, especially the board of directors. Less sense in achieving the meaning and values of work amongst corporate leaders lead to more cronyism scandals occurring in corporations (Johnson and Mitton, 2003) as well as political connections in managing corporations (Gul, 2006; Bliss *et al.*, 2011). These findings suggest that the much improved corporate governance rules are not effective in solving the existing problems. Thus, there is a need to look for an alternative solution to overcome the problem. Arfah and Aziuddin (2008) have suggested that, by treating the organisation as a separate entity, the gap between the functions of ownership and management are widened. Thus, it encouraging more moral hazard behaviour or agency related problems since an organization is typically shaped up by the attitude, values and vision of a corporate leader. Thus, there is a scope for corporate leader behaviour to influence the quality of financial reporting or quality of corporate governance in place. Therefore, this study intends to fill up the void by considering corporate leader behaviour as one of the significant factors influencing the quality of financial reporting. The main objective of this research is to determine the role and influence of corporate leader values on corporate governance mechanisms and financial reporting quality.

1.1 Inner-Out Approach of Corporate Leader Values

The role of corporate leader values on corporate governance mechanisms and financial reporting quality is supported by spiritual leadership theory, workplace spirituality theory, stewardship theory and human governance concept. Fry (2003) argued that sense of spirituality of corporate leader can be developed through an intrinsic motivation that incorporates vision, faith, and altruistic love. When the corporate leader has a strong sense of spirituality, he tends to influence other corporate members through setting a fair corporate vision for all stakeholders, build a strong faith which then create a sense of huge effort in doing works and create a healthy corporate culture with positive values like humility, integrity, loyalty, forgiveness, and honesty. Then, it results in increasing sense of spiritual survival in terms of sense of calling and membership which is needed by all corporate members. Sense of calling is a sense transcendence, being called or sense of vocation which is explains about a deep interest in and satisfaction with the work, see work as an important part of life and ready to work for extra mile in order to achieve an excellent result as well as to meet their satisfaction. Spiritual leadership theory and workplace spirituality proposed a strong argument that positive outcomes can be achieved by corporation in terms of organisational commitment, productivity, continuous improvement, and presenting a quality of financial reporting.

Stewardship theory assumes a strong relationship between the success of corporation and the owners' satisfaction (Donaldson and Davis, 1991; Davis *et al.*, 1997). Thus, a steward tends to protects and maximises shareholders wealth through achieving a firm performance as well as presenting quality of financial reporting. An intention, behaviour, values and attitudes of corporate stewards to act for the best interest of their owners are transforming from a sense of intrinsic motivation to achieve intangible rewards like opportunity for growth, achievement, affiliation, and self-actualisation. Corporate stewards also behave based on a strong feel of membership in a particular organisation by accepting organisation's mission, vision and objectives or known as organisational identification (organisation commitment). As a result, they are motivated to work harder on behalf of the organisation. As a spiritual leader and as a steward to a corporation, this corporate leader has a strong principled value with a high sense of commitment to corporate success and a deep sense of cooperation with corporate management in sharing quality of financial reporting to stakeholders. As the centre element or heart of an organization (Arfah and Aziuddin, 2008), the role of human or man or specifically corporate leader is very important because he has a significant responsibility to shape and direct a corporation in providing interests to stakeholders. Human governance concept is viewed as an internal mechanism, value-based, principle-based, inside-out approach, encompassing the traits of values, and ultimately to develop a corporate culture based on integrity and trust among corporate people. This healthy culture is seen as the soul of corporation which gives an internal strength to corporate governance system to be effective in preparing quality of financial reporting.



2. RELATED RESEARCH AND HYPOTHESES DEVELOPMENT

2.1 Corporate Governance Mechanisms and Financial Reporting Quality

2.1.1 Board Characteristics and Earnings Management

Board Independence

The ability of board to be an effective monitor depends on their independence from company management in making decisions (Beasley, 1996; Davidson *et al.* 2005). Independent directors are expected to be objective and transparent in fulfilling their responsibility towards the corporate goal. Thus, the independence of the board should be the important characteristic in facilitating corporate governance to function effectively. Most prior researchers supported that independence of board has significant influence in increasing the quality of financial reporting. They found that board independence is negatively associated with earnings management (Klein, 2002; Xie *et al.*, 2003; Davidson *et al.*, 2005; Hutchinson *et al.*, 2008; Visvanathan, 2008; Jaggi *et al.*, 2009; Lin and Hwang, 2010). The above evidences inform that board independence plays a crucial role in corporate governance as effective monitor over opportunistic behaviour among managers. However, some studies showed that board independence was insignificant correlated with earnings management such as Park and Shin (2004), Norman *et al.* (2005), Abdul Rahman and Mohamed Ali (2006) and Ghosh *et al.* (2010). There are some reasons and arguments to these inverse relationships. It may be the power of management or executive directors are dominant over the board of directors even though its composition complies with the principle of corporate governance (Dechow *et al.* 1996). It is expected that the higher board independence will assist a company to disclose a high quality of financial reporting or low earnings management. Based on the above discussion, the study proposes the following testable alternative hypothesis:

H_{1A} : There is a negative association between board independence and earnings management.

Board Size

Prior research has documented that a smaller board size may be related to the performance of the company (Yermack, 1996) whereas with a larger board size there is more tendency for financial reporting fraud to occur (Beasley, 1996). However, Beasley and Salterio (2001), Ghosh *et al.* (2010) and Abed *et al.* (2012) found that a larger board is more efficient in monitoring the manipulation of earnings report activities because they argued that a larger board has more expertise, skills and knowledge to fulfill its responsibility. However, Abdul Rahman and Mohamed Ali (2006) found the smaller board was more effective in monitoring and overseeing the financial reporting system and could prevent earnings management activities. It is consistent with the findings by Yermack (1996) and Beasley (1996) where they argued that a larger board did not improve the quality of corporate governance. Furthermore, Xie *et al.* (2003) and Peasnell *et al.* (2005) found a negative association between earnings management and board size. Therefore, the study proposes the following testable alternative hypothesis:

H_{2A} : There is a negative association between board size and earnings management.

CEO Duality

CEO duality or combination position of CEO and chairman is expected less independence than separation between both positions. The roles of board of directors' chairman include the conduct of the board meeting, monitoring the process of selection, evaluation and compensation of the CEO (Lin and Hwang, 2010). Jensen (1993) argued that CEO duality function provides a high potential for conflict of interest since CEO has to chair the board meeting and at the same time needs to perform the oversight function. He suggested that the function of CEO and chairman of the board should be separated to enhance the effective role of monitoring. However, stewardship theory argued that shareholders interests are maximised when CEO also acts as the chairman of the board because executive director or manager tends to serve as steward in carrying out his/her responsibility with intention to provide interest to all



stakeholders, especially shareholders (Donaldson and Davis, 1991; Davis *et al.*, 1997). According to Dechow *et al.* (1996), one of the company characteristics which normally are involved in manipulating earnings is when CEO at the same time serves as chairman of the board. Klein (2002) supported that the board of directors is effective in monitoring the corporate financial reporting process if it is independent from chief executive officer (CEO). Several past studies showed inconclusive findings about the effect of CEO duality on earnings management. Research conducted by Norman *et al.* (2005) supported that the company which has combined the position of CEO and chairman of board of directors tends to manipulate earnings report. Whereas Johari *et al.* (2009); Ghosh *et al.* (2010) and Abed *et al.* (2012) failed to find a significant relationship between the existences of CEO-Chairman duality and earnings management activities. Based on the above arguments the study proposes the following testable alternative hypothesis:

H_{3A} : There is a positive association between CEO duality and earnings management.

2.1.2 Audit Committee Characteristics and Earnings Management

Audit Committee Independence

Independent non-executive director is the important member to increase independence level of audit committee. It is expected to perform more effectively and objectively when free from any personal biases resulting from financial or personnel relationships with the management. Hence, independence of audit committee is a critical factor in monitoring role to ensure management duly performs its responsibility to the shareholders (Menon and Williams 1994). McMullen and Raghunandan (1996) found that the companies which do not have independent non-executive director members in the audit committee tend to face financial reporting problems. They also found the companies which have external director members in the audit committee tend to avoid manipulation of earnings. The effect of audit committee independence on earnings management has been examined in most of the previous studies (Klein, 2002; Abbott *et al.* 2004; Bedard *et al.*, 2004; Davidson *et al.*, 2005; Hutchinson *et al.*, 2008; Lin and Hwang, 2010). These studies supported that independence of audit committee effectively prevent earnings management activities. However, some empirical researches do not support the negative effect of an independent audit committee on earnings management as shown by Xie *et al.* (2003), Abdul Rahman and Mohamed Ali (2006), Baxter and Cotter (2009) and Ghosh *et al.* (2010). Abdul Rahman and Mohamed Ali (2006) argued that an independent audit committee would not able to function effectively in a situation where management has more dominance over certain board matters. Based on the above arguments, the study proposes the following testable alternative hypothesis:

H_{4A} : There is a negative association between audit committee independence and earnings management.

Audit Committee Expertise

Panel practitioners such as Blue Ribbons Committee (1999), Cadbury Committee (1992) and regulators like SEC (2000), Sarbanes-Oxley Act (2002) and MCCG (2007) propose that each member of audit committee has financial literacy and at least one should be a member of an accounting association or body in order to enhance the effectiveness of the audit committee. The study done by Sori *et al.* (2008) support that Malaysian audit committee chairman perceive audit committee will be effective if its member has certain characteristics such as sophisticated accounting knowledge, review of financial statements, auditor independence and are good in management and internal control. Audit committee member who has the knowledge and expertise in auditing and accounting has high tendency to exercise true and fair judgement during monitoring the financial reporting process (Kalbers and Forgyat, 1993) and tend to support auditor in overcoming the dispute between client and management (DeZoort and Salterio, 2001). Empirical research by Xie *et al.* (2003) also showed that board and audit committee who has expertise of its members either related to corporate or finance is effective in preventing earnings management activities. Other studies which documented the significant effect of audit committee expertise in overseeing activities of earnings management are Bedard *et al.* (2004) and Baxter and Cotter (2009). However, Ghosh (2010) failed to show a significant relationship between audit committee expertise and earnings management. Most of the



above discussions show a strong negative relationship between expertise of audit committee and earnings management, thus the study proposes the following testable alternative hypothesis:

H_{5A} : There is a negative association between audit committee expertise and earnings management.

2.1.3 Ownership Structure and Earnings Management

Insider Ownership

Insider ownership is also known as managerial ownership and it is expected to influence the quality of financial reporting. Jensen and Meckling (1976) argued that agency conflicts between managers and corporate owners can be reconciled if managers owned some portion of interest in their companies. By offering some percentage of corporate shares, managers are motivated to manage corporation effectively and then agency cost can be reduced. Furthermore, the process of financial reporting is more efficient through effective cooperation between management and board of directors. Generally, it is expected that insider ownership may reduce the activities of manipulation earnings among company management. Warfield *et al.* (1995) reported managerial ownership is negatively correlated to magnitude of accounting accrual adjustments whereas it is positively associated with earnings' explanatory power for returns whereas Ballesta and Garcia-Meca (2005) found higher insider ownership is an effective characteristic to corporate governance and it contributed to high quality financial reporting. In the Malaysian context, Norman *et al.* (2005) reported that earnings management is negatively related to management ownership and Mohd Ali *et al.* (2008) supported that managerial ownership is negatively associated with earnings management. However, Johari *et al.* (2009) showed the company which has ownership by managers more than 25% may increase the potential to manage earnings and Hutchinson *et al.* (2008) showed executive shareholding is positively associated with earnings management. They concluded that increasing of insider ownership may motivate manager to manage earnings. However, Ghosh *et al.* (2010) and Abed *et al.* (2012) documented that there was insignificant difference between director ownership and earnings management. Current study by Farooq and Jai (2012) also found ownership concentration by manager has no significant relationship with earnings management. From the above discussion, it is found that findings of prior studies regarding the influence of insider ownership on financial reporting quality showed inconsistency of relationship direction. Hence, the study proposes the following testable alternative hypothesis:

H_{6A} : There is a negative association between insider ownership and earnings management.

Outsider Ownership

Independent non-executive directors are expected to be an effective monitor on management behaviour in corporation. MCGG (2007) suggests the significant share ownership by company directors means non-independent directors. Thus, it is assumed that outsider ownership may reduce an efficiency function of outside directors or independent non-executive directors in overseeing company management behaviour due to decrease of directors' independence. However, Hashim (2009) found outsider ownership among Malaysian corporations is positively significant relationship with earning quality and is negatively associated with financial distress as documented by Abdullah (2006). Beasley (1996) supported that outside director ownership was effective to prevent financial statement fraud. Therefore, the study proposes the following testable alternative hypothesis:

H_{7A} : There is a negative association between outsider ownership and earnings management.

Institutional Ownership

Institutional investor is argued to be an important monitor for a corporation. Normally, institutional investors own larger holdings equity than individual investors in company, thus they may provide more potential to influence company management. According to Solomon and Solomon (2004), institutional investor is another powerful corporate governance mechanism that can monitor company management in order to align interest between management and shareholders. Thus, it is expected that institutional owners becomes effective monitors on



management behaviour towards corporate goals. Dechow *et al.* (1996) concluded that the company which is less likely to have outside blockholder tends to increase earnings management. Hadani *et al.* (2011) found that institutional investors are effective monitors on earnings management activities in the company whereas Velury and Jenkins (2006) reported the institutional ownership is positively related to the quality of earning. However, they found that concentrated institutional ownership is negatively correlated with earning quality. Farooq and Jai (2012) showed that institutional ownership, whether local or foreign, has significant association with earnings management. Inconsistent result was reported by Siregar and Utama (2008) who found insignificant relationship between institutional ownership and the type of earnings management. From the above results and discussion, it can be addressed that institutional ownership provides a significant influence to company in presenting the financial reporting quality. Thus, the study proposes the following testable alternative hypothesis:

H_{8A} : There is a negative association between institutional ownership and earnings management.

2.2 Workplace Spirituality, Effective Corporate Leader and Financial Reporting Quality

Workplace spirituality can influence corporation to enhance the effectiveness of corporate leadership (Abdullah *et al.*, 2009). This healthy corporate culture can assist corporate leader manages a corporation effectively. According to Duchon and Ashmos (2005) workplace spirituality consists of corporate leaders and corporate employees who have an inner life that nourishes and is nourished by meaningful work. The concept of workplace spirituality is the holistic theory of spirituality because it tends to incorporate a sense of spirituality of corporate leader, sense of spirituality of teamwork and sense of spirituality of corporation. It is essentially consistent with the concept of human governance which is introduced by Arfah and Aziuddin (2008). From the concept of human governance, a corporate leader and other corporate members are important human in a corporation because they are responsible to energise the inner strength of corporate governance mechanisms in governing corporation. The human governance concept argued that a healthy corporate culture that based on integrity and trust among corporate members is as a soul to corporation where it can gives a deep sense of consciousness to corporate leader (CEO), directors, and other corporate management to be ethical without sense of self interest while governing and managing corporation. Thus, they tend to work hard in order to serve for their stakeholders especially to provide quality information in financial reporting. There are three factors that can essentially nourish values for corporate leaders: inner life, meaning at work and sense of community (Ashmos and Duchon, 2000; Duchon and Ashmos, 2005).

2.2.1 Corporate Leader Values

Inner Life

Inner life is the core and most important element in a human being because it is related to a deep sense of human self in terms of vision, meaning and values. Human being has a duality in nature; body (physical) and soul (spirit) (Al-Attas, 1995, Al-Mahdi, 2004, Zohar and Marshall, 2004, Haque and Mohamed, 2009). Both elements are interconnected because human behaviours and actions are resulting from a sense of inner life of human self. There are many studies in the field of psychology (Haque and Mohamed, 2009), religious studies (Haque and Mohamed, 2009), management (Quatro *et. al.*, 2007; Covey, 1995) addressed that human self is the significant element to influence human behaviours, actions, attitudes and personality in human life as well as in their working life. Thus, corporate people attributes (outer-behaviour, attitudes) naturally comes from a deep sense of their values (inner-values) (Al-Jamal, 1977; Zohar and Marshall, 2004). A spiritual corporate leader has a clear vision and has a high intention to influence and motivate their subordinates together in achieving the corporate goals as well as meeting their stakeholders' interest. With a deep sense of interconnectedness, engagement and responsibility, corporate leader has a power of self-governance, ethical and integrity in doing works and monitoring others' works. He/she does not agree with any activities that relating to manipulation of earnings figures or misrepresentation of financial reporting occur in corporation. Thus, it is expected that sense of spirituality of corporate leader may influence corporate governance to be more effective in preventing earnings management activities. Past studies supported



that the spiritual health of a corporate leader is positively related with intrinsic, extrinsic and work rewards satisfaction (Kolodinsky *et al.*, 2007), physical and mental health as well as job satisfaction (Sprung *et al.*, 2012) and higher work productivity (Garcia-Zamor, 2003). The current study by Fry *et al.* (2011) revealed that spiritual well-being (calling and membership) mediates the relationship between spiritual leadership with the organisational performance and commitment.

Meaning at Work

Meaning at work is interconnected with sense of inner life of corporate leader. Initially, corporate leaders bring their spirit, values, personality to the workplace. A sense of deep vision, value and meaning at work is important to corporate leaders because it can influence the way they manage and organise a corporation (Zohar and Marshall, 2004; Reave 2005). When corporate leaders have a sense of meaning at work, they feel that working is very important in their life and sense of their spirit also can be energised by the works in which they involved. Every day, they enjoy and look forward to coming to work. They have a deep sense of interconnectedness of life and all its business organisations, workplace community and the whole society. They feel a strong connection between their soul and work as well as sense of calling and vocation to work. This feeling is manifested by a deep sense of vision; there is to provide benefits and share interest to community and the whole society. Meaning at work is a significant value to a corporate leader since it can help him/her to be an efficient corporate leader in organising corporation (Abdullah *et al.*, 2009). It is impossible for corporate leaders who have a sense of meaning at work to engage in wrong behaviour and unethical actions in the workplace. Thus, it is expected that a corporate leader who has a high sense of meaning at work can influence corporate management and directors to be more integrity and honesty in monitoring unethical activities relating to management of earnings figures.

Sense of Community

Sense of community is the third important element to workplace spirituality at the individual level as introduced by Ashmos and Duchon (2000). Sense of community and connection is a nature feeling of human being since people cannot survive properly without connecting with others. However from the aspect of workplace spirituality, corporate leader and members who have a sense of community want to feel connected to work and they want to feel connected to each other at the workplace. This feeling is an essential of spiritual development. As a result, corporate leader tend to serve others more than serve for him while organising a business corporation. This situation is also can be explained by the stewardship theory arguments; a corporate leader serves as a steward for a corporation where he has a high motivation to conduct business operation on behalf of stakeholders (McCuddy and Pirie, 2007). From the human governance concept, the sense of community and connection of corporate leader becomes a soul for corporation which can energise an inner strength of corporate leader to manage corporation for the benefits of corporate owners, corporation, workplace community and the whole society. Most previous studies support the positive impact of workplace spirituality on corporate performance (Duchon and Plowman, 2005; Marques, 2008; Karakas, 2009; Fry *et al.*, 2011), corporate commitment (Milliman *et al.*, 2003; Kolodinsky *et al.*, 2007; Rego and Cunha, 2008), jobs satisfaction (Pawar, 2009; Sprung *et al.*, 2012) and productivity (Garcia-Zamor, 2003). Thus, it is expected that a sense of community among corporate leaders also can influence other directors and managers to serve for the best interest of corporate users with providing quality information in the corporate financial reporting.

Hence, the study proposes the following testable alternative hypotheses to test the three factors of workplace spirituality at the corporate leader level: inner life (IL), meaning at work (MW) and sense of community (SC) on corporate governance mechanisms and earnings management.

H_{9A1} : The corporate governance mechanisms will mitigate earnings management, especially among corporate leaders with a high sense of inner life.

H_{9A2} : The corporate governance mechanisms will mitigate earnings management, especially among corporate leaders with a high sense of meaning at work.



H_{9A3} : The corporate governance mechanisms will mitigate earnings management, especially among corporate leaders with a high sense of community.

2.2.2 Team Values and Corporate Values

Corporate culture is a significant environment to support a corporate leader manages and organise a corporation efficiently towards the corporate goals. In the study, it is expected that the whole corporate culture can be developed by the integration of sense of team values and corporate values. Team values are related to the perception on positive works values in terms of sense of teamwork conscience, sense of connection between goals and missions of team members and corporation, sense of teamwork concerns, caring and encouraging team members and community. Daniel (2010) found that the organisation which encouraged workplace spirituality tends to have an effectiveness team in terms of trust, creativity and respect. While corporate values are related to the perception on positive corporate values like sense of corporate conscience, sense of connection between corporate members' goals and corporation's goals, corporate concerns and cares of corporate members and community. Team values and corporate values are transforming by sense of spirituality among team members and corporate members. It means that, both values explain about sense of integrity, honesty and ethical of team and corporate members. As an integrity person, each member tends to be more ethical and committed in completing the works. Thus, it is expected that sense of team values as well as corporate values have a more potential to enhance quality of corporate governance function in presenting quality of financial reporting.

Hence, the study proposes the following testable alternative hypotheses to test one factor of workplace spirituality at the team level as team values (TV) and one factor at the corporate level as corporate values (CV) on corporate governance mechanisms and earnings management.

H_{9A4} : The corporate governance mechanisms will mitigate earnings management, especially among companies with a high sense of team values.

H_{9A5} : The corporate governance mechanisms will mitigate earnings management, especially among companies with a high sense of corporate values.

3. METHODOLOGY

3.1 Source of Data

The present study is a cross sectional and uses a quantitative approach. The data is retrieves from two sources; (1) the primary data is acquired from the structured questionnaire which is distributed to corporate leader in 2010; (2) the secondary data is collected from the annual reports of Malaysian listed companies for 2008, 2009 and 2010. The primary data is concerned with perception of corporate leader values by the corporate leader especially Chief Executive Officer (CEO) or Managing Director (MD). The questionnaire uses a self evaluated approach and it is distributed to Malaysian corporate leaders by hand. They are given a reasonable time to complete the questionnaire. Then, the completed questionnaires are collected from these corporate leaders by hand. The second source of data is annual reports of companies that are available in website of Bursa Malaysia (<http://www.bursamalaysia.com>). The secondary data are manually collected from annual reports which comprise financial and non-financial data.

3.2 Population and Sample Selection

The population of the study consists of non-financial listed companies at Main Market in Bursa Malaysia until 2010. The sample of the study is based on the questionnaires responded to and returned by corporate leaders of these companies. Table 3.1 and 3.2 shows the population or sampling frame of the study and the distribution of



sample by industry respectively. Table 3.1 shows sampling frame of the study consisting of seven main industries in Malaysia that are listed at Main Market at Bursa Malaysia in 2010. Finance industries such as banking, financial institutions, and finance and investment companies are excluded since they are governed by highly regulated regulations (Klein 2002; Abdul Rahman and Mohamed Ali, 2006; Norman *et al.* 2007). In the Malaysian context, the related regulation is Banking and Financial Institutions Act 1989. Thus, the total of listed company remaining in sampling frame list until 2010 is 768 companies.

TABLE 3.1: Sampling Frame by Industry

Industry	Number of Companies	Percentage
Construction	50	6.51
Customer product	132	17.19
Industrial product	262	34.11
Plantation	41	5.34
Properties	87	11.33
Technology	23	3.00
Trading or Services	173	22.52
Total	768	100

TABLE 3.2: Distribution of Sample by Industry

Industry	Number of Companies	Percentage
Construction	22	17.74
Customer product	45	36.29
Industrial product	38	30.65
Technology	10	8.06
Trading and Services	9	7.26
Total	124	100

Table 3.2 reports distribution of sample by industry based on questionnaire responded to and returned by corporate leaders. The total sample of study is 124 companies which is equal to 16.15% out of population. The highest industry is customer product (36.29%) followed by industrial product (30.65%), construction (17.74%), technology (8.06%) and trading and services (7.26%). However, four companies have incomplete financial and non-financial data and these companies are excluded from the sample of study. Hence, the total sample of study is 120 companies.

3.3 Measurement of Variables

The study has three main variables. Firstly, dependent variable is earnings management. Secondly, independent variable is corporate governance mechanisms such as board independence, board size, CEO duality, audit committee independence, audit committee expertise, insider or managerial ownership, outsider ownership and institutional ownership. Thirdly, moderating variable proposed is sense of spirituality at workplace factors. The study concentrates on earnings management activities in identifying the level of financial reporting quality for the company. Consistent with prior empirical research the study uses discretionary accruals (DA) as a proxy for earnings management (Klein, 2002; Norman *et al.*, 2005; Abdul Rahman and Mohamed Ali, 2006; Ghosh *et al.*, 2010). Large discretionary accruals indicate low quality of financial reporting. The study applied the model which is initially proposed by Jones (1991) and subsequently modified by Dechow *et al.* (1995). These models approach



are more powerful to detect the manipulations of revenue and bad debt (Peasnell *et al.*, 2000). The modified Jones model (Dechow *et al.*, 1995) is used in the study. Basically, the model separates the total discretionary accruals (TA) into two components of non-discretionary accruals (NDA) and discretionary accruals (DA). The component of discretionary accruals is deemed to reflect the portion of earnings management.

TABLE 3.3: Definition, Measurement and Operationalisation of Variables

Variable [Acronym]	Definition	Measurement and Operationalisation	References
Dependent Variable			
Earnings management [DA]	Discretionary accruals	The absolute value of discretionary accruals	Jones (1991); Dechow <i>et al.</i> (1995)
Independent Variable			
Board independence [BDIND]	The composition of outside director in board of directors.	The proportion of independent non-executive directors to the total number of directors on the company's board.	Norman <i>et al.</i> , (2005); Lin and Hwang (2010)
Board size [BDSZE]	Size of board of directors.	Total numbers of directors on the board of the company.	Yermack (1996); Abdul Rahman and Mohamed Ali (2006)
CEO duality [CEOD]	The positions of CEO and chairman of the board is hold by the same person.	Dichotomous with "1" if the chairman and CEO are the same person and "0" otherwise.	Klein (2002); Norman <i>et al.</i> (2005)
Audit committee independence [ACIND]	The composition of outside director in audit committee.	The proportion of independent non-executive directors to the total number of directors on the audit committee.	Abdul Rahman and Mohamed Ali (2006); Baxter and Cotter (2009)
Audit committee expertise [ACEXP]	Composition of accountants in audit committee.	The proportion of accountants to the total number of directors on the audit committee.	Malaysian Code of Corporate Governance (2007)
Insider ownership [INOWN]	Ownership by executive and non-independent non-executive directors of the company.	The percentage of shares owned by executive and non-independent non-executive directors of the company.	Mohd Ali <i>et al.</i> (2008); Ghosh <i>et al.</i> (2010).
Outsider ownership [OUTOWN]	Ownership by independent non-executive directors of the company.	The percentage of shares owned by independent non-executive directors of the company.	Hashim (2009)
Institutional ownership [INSTOWN]	Ownership by institutional investors.	The percentage of shares owned by five largest institutional investors	Abdul Wahab <i>et al.</i> (2007)
Moderating Variable			
Spirituality at workplace [SWP]	Sense of spirituality of corporate leader including teamwork and corporation.	Using a seven-point Likert scale of 1 for strongly disagree through to 7 for strongly agree	Ashmos & Duchon (2000); Fry (2003)
Control Variable			
Company size [SIZE]	Size of the company	Natural logarithm of total assets	Klein (2002)
Company leverage	Leverage of the company	The ratio of total liabilities to	DeZoort and Salterio



[LEV]		total assets	(2001)
Return on assets	Return on total assets of the	The ratio of profit before tax to	Abdul Rahman and
[ROA]	company	total assets	Mohamed Ali (2006)
Audit quality	The quality of external	Coded "1" if the company	DeAngelo (1981)
[AUDQ]	auditors	audited by Big 4 and "0"	
		otherwise.	

The estimation of discretionary accruals (DA) involves three steps. In step one, a cross sectional regression of total accruals on change in revenue and plant, property and equipment (all scaled by lagged total assets) is run to obtain estimates of coefficients a , b and c for each industry. This study uses t as time which refers to year 2009 and 2010 and $t-1$ refers to year 2008 and 2009 respectively.

$$TA_t / A_{t-1} = a (1 / A_{t-1}) + b \Delta REV_t / A_{t-1} + c PPE_t / A_{t-1} + \delta_t \quad (1)$$

where, TA_t = Total accruals at time t ;
 A_{t-1} = Total assets at time $t-1$;
 ΔREV_t = Change in revenues at time t and;
 PPE_t = Total plant, property and equipment at time t .

In step two, the estimated coefficients a , b and c are substituted into the following equation's coefficients (α , β and γ) to obtain non-discretionary accruals (NDA) for each company.

$$NDA_t / A_{t-1} = \alpha (1 / A_{t-1}) + [\beta (\Delta REV_t - \Delta REC_t) / A_{t-1}] + \gamma (PPE_t / A_{t-1}) \quad (2)$$

where, NDA_t = Non-discretionary accruals at time t and;
 ΔREC_t = Change in receivables at time t .

Lastly in step 3, the discretionary accruals (DA) are determined as;

$$DA = TA_t / A_{t-1} - NDA_t / A_{t-1} \quad (3)$$

3.4 Regression Model

The study uses hierarchical multiple regression analysis or sequential multiple regression analysis to determine the influence of spirituality at workplace factors on the relationship between corporate governance mechanisms and earnings management. There are three steps that should be followed in order to test the moderating effects for the proposed research model.

Model 1:

$$DA = \beta_0 + \beta_1 BDIND + \beta_2 BDSIZE + \beta_3 CEOD + \beta_4 ACIND + \beta_5 ACEXP + \beta_6 INOWN + \beta_7 OUTOWN + \beta_8 INSTOWN + \beta_9 SIZE + \beta_{10} LEV + \beta_{11} ROA + \beta_{12} AUDQ + \varepsilon$$

Model 2:

$$DA = \beta_0 + \beta_1 BDIND + \beta_2 BDSIZE + \beta_3 CEOD + \beta_4 ACIND + \beta_5 ACEXP + \beta_6 INOWN + \beta_7 OUTOWN + \beta_8 INSTOWN + \beta_9 SWP + \beta_{10} SIZE + \beta_{11} LEV + \beta_{12} ROA + \beta_{13} AUDQ + \varepsilon$$

Model 3:

$$DA = \beta_0 + \beta_1 BDIND + \beta_2 BDSIZE + \beta_3 CEOD + \beta_4 ACIND + \beta_5 ACEXP + \beta_6 INOWN + \beta_7 OUTOWN + \beta_8 INSTOWN + \beta_9 SWP + \beta_{10} BDIND*SWP + \beta_{11} BDSIZE*SWP + \beta_{12} CEOD*SWP + \beta_{13} ACIND*SWP + \beta_{14} ACEXP*SWP + \beta_{15} INOWN*SWP + \beta_{16} OUTOWN*SWP + \beta_{17} INSTOWN*SWP + \beta_{18} SIZE + \beta_{19} LEV + \beta_{20} ROA + \beta_{21} AUDQ + \varepsilon$$

Where;

*Dependent variable:*

DA = Discretionary accruals

Independent variables:

BDIND = Board independence

BDSZE = Board size

CEOD = CEO duality

ACIND = Audit committee independence

ACEXP = Audit committee expertise

INOWN = Insider ownership

OUTOWN = Outsider ownership

SWP = Spirituality at workplace

Interaction terms:

BDIND*SWP = Interaction between board independence and spirituality at workplace

BDSZE*SWP = Interaction between board size and spirituality at workplace

CEOD*SWP = Interaction between CEO duality and spirituality at workplace

ACIND*SWP = Interaction between audit committee independence and spirituality at workplace

ACEXP*SWP = Interaction between audit committee expertise and spirituality at workplace

INOWN*SWP = Interaction between insider ownership and spirituality at workplace

OUTOWN*SWP = Interaction between outsider ownership and spirituality at workplace

Control variables:

SIZE = Size of company

LEV = Leverage of company

ROA = Return on assets of company

AUDQ = Audit quality

 ε = Error term

4. EMPIRICAL RESULTS

4.1 Factor and Reliability Analysis

Table 4.1 shows seven new factors are formed after dropping 24 items from initial factors. One item of inner life factors is deleted then forms two new factors, namely spiritual health (SH) and spiritual values (SV) which have 2 items each respectively. Meaning at work (MW) dropped all 9 items. This situation occurs because the MW items have the reliability coefficients below than 0.7, meaning no consensus among respondents with regard to MW items. This result indicates that the Malaysian corporate leaders, especially CEO, have less sense of meaning at work from the perspective of workplace spirituality that proposed by Ashmos and Duchon (2000).

TABLE 4.1: Transformation of Initial Factors to Form a New Factor of Workplace Spirituality

Level	Initial factor	Item before FA	Item dropped	Item after FA	New factor name	No. of item
Individual	Inner life	5	1	4	Spiritual health	2
					Spiritual values	2
	Meaning at work	9	9	0	Nil	0
					Recognition &	3



	Sense of community	10	3	7	Appreciation	
					Sense of community	4
Team	Team values	12	8	4	Team values	4
					Corporate values	4
Corporate	Corporate values	11	3	8	Corporate concern	4
Total		47	24	23		23

Notes: FA - factor analysis

These results suggest that the related MW items used are less suitable to evaluate sense of meaning at work among Malaysian corporate leaders even it shows high reliability coefficients in other countries. Generally, Malaysian people tend incorporate religion in their life whereas Western people are more likely to separate religion and their daily life. Thus, the proposed MW items used are less relevant to Malaysian corporate leaders. Sense of community has dropped three items to form two new factors: recognition and appreciation (RA) which has 3 items while sense of community (SC) has 4 items. 8 items are dropped from team values (TV) retaining only 4 items. Lastly, the remaining items for corporate level are 8 where it is split into two new factors. These factors are corporate values (CV) and corporate concern (CC) which contains 4 items each respectively.

TABLE 4.2: Reliability Coefficients for Workplace Spirituality Factors

Factor	New factor	Number of items	Cronbach's alpha
1	Corporate Concern (CC)	4	0.788
2	Sense of Community (SC)	4	0.782
3	Team Values (TV)	4	0.767
4	Corporate Values (CV)	4	0.784
5	Recognition and Appreciation (RA)	3	0.782
6	Spiritual Health (SH)	2	0.808
7	Spiritual Values (SV)	2	0.792
Total items		23	0.736

Table 4.2 shows that the reliability coefficients for seven factors of workplace spirituality are in the ranges of 0.767 to 0.808. According to Hair *et al.* (2010) the generally agreed upon lower limit for Cronbach's alpha is 0.70. However, for exploratory research, an acceptable lower limit is 0.60. Thus, it can be concluded that these measures of workplace spirituality factors possess sufficient reliability.

4.2 Descriptive Statistics

4.2.1 Descriptive Statistics for Workplace Spirituality Factors

Table 4.3 presents the mean and standard deviation for seven factors of workplace spirituality in three levels: individual level, team level and corporate level. At the individual level of a corporate leader, spiritual values (SV) and spiritual health (SH) are amongst the highest mean scores with 6.1129 and 5.9798 respectively. It suggests that the sense of spirituality or inner life of Malaysian corporate leaders is at the moderate level. However, the sense of spiritual values has more potential to be influenced by inherent bias in instrument because it involves sensitive questions. It is normal if an individual corporate leader tends to evaluate or show him as a better corporate leader while responding to daily spiritual practices questions. Another two factors of workplace spirituality at an individual of corporate leader level, sense of recognition and appreciation (RA) and sense of community (SC) with scores of 5.6747 and 5.7923 respectively. It reveals that the relationship of Malaysian corporate leaders with the



workplace community in terms of sense of recognition and appreciation (RA) and sense of community (SC) is still at the low level.

TABLE 4.3: Descriptive Statistics for Workplace Spirituality Factors

Factor	Factor name	Mean	Median	Standard Deviation
1	Corporate Concern (CC)	5.8649	6.0	0.49735
2	Sense of Community (SC)	5.7923	6.0	0.52646
3	Team Values (TV)	5.7379	6.0	0.50188
4	Corporate Values (CV)	5.6915	6.0	0.45208
5	Recognition & Appreciation (RA)	5.6747	6.0	0.49105
6	Spiritual Health (SH)	5.9798	6.0	0.49139
7	Spiritual Values (SV)	6.1129	6.0	0.51734

Notes: All items used a 7-point Likert scale with (1 = Strongly disagree and 7 = Strongly agree)

At the team and corporate levels, sense of team values (TV) and corporate values (CV) are among the lowest mean scores with 5.7379 and 5.6915. However, the mean score of corporate concern (CC) is slightly higher with a score of 5.8649. It shows that the Malaysian corporate leaders have a low sense of team values and corporate values. It is important to highlight that the items used to measure team values (TV), corporate values (CV) and corporate concern (CC) are a more general evaluation because they refer to team and corporation as a whole with no direct connection to a individual corporate leader. It shows detachment between team and corporation and individual corporate leader. Thus, the corporate leaders tend to answer the related items with no sense of belonging. In addition, questions at the team and corporate levels are too philosophical compared to questions at the individual level.

4.2.2 Descriptive Statistics for Corporate Governance Mechanisms

Table 4.4 presents the descriptive statistics results for continuous category of variables followed by Table 4.5 which shows the results of descriptive statistics for dichotomous variables. The total number of observations is 240 with 120 observations or companies from 2009 and 2010 respectively. As reported in Table 4.4, the average magnitude for discretionary accruals (DA) among Malaysian listed companies in 2010 is higher than in 2009 with score values of 0.0765 and 0.0358 respectively. The ranges of DA magnitudes for both years is from -0.83 to 0.73. It is a similar condition for average score of discretionary current accruals (DCA). Year 2010 is higher than 2009 with scores of -0.0212 and 0.0080 respectively with range between -0.84 to 0.43. These results inform that most Malaysian corporations practice earnings management even though the current level of DA is higher than in 2005 as reported by Norman *et al.* (2005) with score -0.007. However, the current magnitude of DCA is relatively low compared to 2006 as documented by Abdul Rahman and Mohamed Ali, (2006) with score of 0.0468 and in another country shows magnitude of 0.0105 as reported by Xie *et al.* (2003).

Average board independence (BDIND) for 2009 and 2010 is 44.09% and it's higher than the minimum requirement of MCGG (2007) which is to have at least one-third of the board membership independent non-executive directors. The minimum of board independence is 29% and the highest is 75%. Average size of board of directors among Malaysian listed companies is seven directors. It is a reasonable size and consistent with the argument by Jensen (1993) that the maximum size of board is seven or eight. He also suggests the smallest board should comprise four directors and the biggest board thirteen directors. Average audit committee independence (ACIND) for both years is 88.40%. It means that the audit committees of Malaysian corporations comprise majority of independent non-executive directors and meets the suggestion by MCGG (2007). Some companies have fully independent non-executive directors in their audit committee. For audit committee expertise (ACEXP) in all years, 36.15% of audit committee members are qualified accountants or member of an accounting body. Some audit committees comprise



fully qualified accountants. Share ownership by executive director and non-executive non-independent director (INOWN) averages 37.811% with the highest ownership at 83.05%.

Shares owned by independent non-executive directors (OUTOWN) is about 0.4322% which is not more than the 1% suggesting that outsider interest in Malaysian corporations is still at a low level. The largest portion of shares owned by outside directors is only 7.66%. Average of investment by institutional investors (INSTOWN) in Malaysian corporations is about 2.55%. However, the highest percentage shares owned by institutional investors in 2010 is much higher than 2009 with percentage ownership of 71.51% and 25.85% respectively. Mean log of total assets for Malaysian corporations is 8.4806 within the ranges between 7.33 and 10.41. The average leverage among Malaysian corporations is 41.43% with ranges from 6% to 136%. It gives a signal that the portion of debt is relatively higher compared to the total assets owned by Malaysian companies. The mean percentage of ROA is 4.89% with its ranges beginning with losses of -57% until maximum returns of 70% suggesting that the Malaysian corporate performance is relatively low.

TABLE 4.4: Descriptive Statistics of Continuous Variables

Variables		Mean	Median	Standard Deviation	Minimum	Maximum
DA (Discretionary Accruals)	2009	0.0358	0.0299	0.17292	-0.83	0.67
	2010	0.0765	0.0684	0.15311	-0.30	0.73
	All year	0.0561	0.0479	0.16424	-0.83	0.73
DCA (Discretionary Current Accruals)	2009	-0.0212	-0.0106	0.12676	-0.84	0.39
	2010	0.0080	-0.0031	0.11096	-0.27	0.43
	All year	-0.006	-0.0050	0.11976	-0.84	0.43
BDIND (Board Independence)	2009	0.4376	0.4286	0.10446	0.29	0.75
	2010	0.4443	0.4286	0.11620	0.20	0.75
	All year	0.4409	0.4286	0.11032	0.20	0.75
BDSIZE (Board Size)	2009	7.4667	7.000	1.86491	4.00	13.00
	2010	7.3167	7.000	1.84247	4.00	13.00
	All year	7.3917	7.000	1.85136	4.00	13.00
ACIND (Audit Committee Independence)	2009	0.8764	1.000	0.15201	0.67	1.00
	2010	0.8917	1.000	0.15032	0.67	1.00
	All year	0.8840	1.000	0.15104	0.67	1.00
ACEXP (Audit Committee Expertise)	2009	0.3535	0.3333	0.17948	0.00	1.00
	2010	0.3694	0.3333	0.18578	0.00	1.00
	All year	0.3615	0.3333	0.18245	0.00	1.00
INOWN (Insider Ownership)	2009	37.6580	36.8450	20.78810	0.00	77.57
	2010	37.9640	37.4035	21.46320	0.00	83.05
	All year	37.8110	36.9219	21.08466	0.00	83.05
OUTOWN (Outsider Ownership)	2009	0.4358	0.020	1.32553	0.00	7.65
	2010	0.4286	0.020	1.28960	0.00	7.66
	All year	0.4322	0.020	1.30485	0.00	7.66
INSTOWN (Institutional Ownership)	2009	2.5323	0.000	5.27261	0.00	25.85
	2010	2.5668	0.000	8.18846	0.00	71.51
	All year	2.5495	0.000	6.87223	0.00	71.51
SIZE (Company Size)	2009	8.4595	8.3885	0.53252	7.33	10.08
	2010	8.5017	8.4110	0.57056	7.48	10.41
	All year	8.4806	8.3930	0.55112	7.33	10.41



LEV	2009	0.4096	0.3783	0.20907	0.06	1.06
(Company	2010	0.4191	0.3740	0.22612	0.08	1.36
Leverage)	All year	0.4143	0.3740	0.21736	0.06	1.36
ROA	2009	0.0442	0.0492	0.12058	-0.49	0.70
(Return on Assets)	2010	0.0537	0.0568	0.12321	-0.57	0.61
	All year	0.0489	0.0537	0.12174	-0.57	0.70

Table 4.5 presents descriptive statistics of two dichotomous variables: CEO duality (CEOD) and audit quality (AUDQ). The result shows that 17 out of 120 (14%) of Malaysia listed companies have duality function of chairman and Chief Executive of Officer (CEO duality) for both 2009 and 2010. It suggests that more than 80% of Malaysian corporations have separated the position of board chairman and CEO. This is consistent with the results by Abdullah (2004). Regarding audit quality (AUDQ), the study finds that half of the Malaysian listed companies are audited by the Big 4 which is about 53.33% or 64 out of 120 companies in 2009 and about 46.67% or 56 out of 120 companies in 2010. This evidence indicated that most Malaysian corporations prefer a high quality audit firm as their external auditors.

TABLE 4.5: Descriptive Statistics of Dichotomous Variables

Variable	All Year (N = 240)		2009 (N = 120)		2010 (N = 120)	
	1	0	1	0	1	0
CEO Duality [CEOD]	34 (14.17)	206 (85.83)	17 (14.17)	103 (85.83)	17 (14.17)	103 (85.83)
Audit Quality [AUDQ]	123 (51.25)	117 (48.75)	64 (53.33)	56 (46.67)	59 (49.17)	61 (50.83)

4.3 Correlations

Pearson correlation analysis is used to determine the size and direction of correlation among variables of the study. Table 4.6 shows the results of coefficients among variables for 120 companies or 240 observations for combined years of 2009 and 2010. As shown in Table 5.9, the range of correlation coefficients among variables is from -0.363 to 0.439 with highest correlation coefficient being between team values (TV) and corporate values (CV). The result suggests that there is no multicollinearity problem since the highest value of coefficient is less than 0.8 (Gujarati, 2009). Discretionary current accruals (DCA) are positively correlated with audit committee independence (ACIND) and return on assets (ROA) at 5 percent level with β coefficient of 0.137 and 0.153 respectively. Board independence (BDIND) is found to be negatively correlated with board size (BDSIZE) and positively correlated with audit committee independence (ACIND). Board size is positively correlated with audit committee independence, outsider ownership (OUTOWN), company size (SIZE) and return on assets (ROA) but negatively correlated with audit committee expertise (ACEXP). The result indicates that the proportion of independent non-executive directors in board is decrease as board size is increased. However, audit committee independence consistently increases with the increase of board independence and board size. Audit committee expertise is positively correlated with audit committee independence suggesting that audit committee has more knowledge and expertise as the proportion of independent non-executive directors in audit committee increased.

Surprisingly, CEO duality shows a positive correlation with audit committee expertise, insider ownership (INOWN), return on assets (ROA) but negatively correlated with company leverage (LEV). With respect to ownership structure, it is found that insider ownership is negatively related to institutional ownership (INSTOWN).



This correlation indicates that the company which has a higher proportion of manager owners tends to reduce the proportion of outside owners in company. It is interesting to note that only institutional ownership (INSTOWN) show a positively correlated with most of workplace spirituality factors such as sense of spirituality values (SV), recognition and appreciation (RA) of corporate leader, corporate value (CV) and corporate concern (CC). The finding reveals that the company which has high spirituality of corporate leader as well as at workplace has more opportunity to get high proportion of institutional ownership (INSTOWN). Hence, it can be as a good external monitor to company management activities.

In terms of workplace spirituality factors, most of the seven factors which consist of spiritual health (SH), spiritual values (SV), sense of community (SC), recognition and appreciation (RA), team values (TV), corporate concern (CC) and corporate values (CV) have positively correlation with each other except for the correlation between spiritual health (SH) and corporate concern (CC). The results indicate that sense of spirituality of corporate leader influence corporate members (team values) as well as the company itself (corporate concern and corporate values) to be more ethical in governing and managing the corporation. With regards to company characteristics, company size is positively correlated with board size (BDSZE), institutional ownership (INSTOWN), company leverage (LEV) and audit quality (AUDQ) and negatively correlated with insider ownership (INOWN). Lastly, audit quality (AUDQ) is positively correlated with company return on assets (ROA). These results suggest that company size (SIZE) is dominance factor in implementing good corporate governance practices.



TABLE 4.6: Pearson Correlation Coefficients among Variables (N=240)

Variables	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20
DA[1]	1																			
DCA[2]	.779**	1																		
BDIND[3]	-.066	-.052	1																	
BDSIZE[4]	.032	.077	-.363**	1																
CEOD[5]	-.047	-.028	-.017	-.125	1															
ACIND[6]	.118	.137*	.344**	.248**	-.024	1														
ACEXP[7]	.031	.095	.085	-.141*	.156*	.156*	1													
INOWN[8]	.044	.089	-.123	-.007	.170*	.115	-.004	1												
OUTOWN[9]	.067	.045	.027	.177*	-.099	-.048	-.014	.073	1											
INSTOWN[10]	-.094	-.122	-.020	.080	.032	-.059	-.009	-.217**	-.047	1										
SIZE[11]	.038	.109	-.099	.373**	-.119	.081	.056	-	-.067	.215**	1									
LEV[12]	-.055	-.077	-.039	-.043	-.182**	.104	.138*	-.219**	-.049	.106	.267*	1								
ROA[13]	.104	.153*	.041	.133*	.129*	-.034	-.039	-.074	-.030	-.016	.176*	-.353**	1							
AUDQ[14]	-.020	-.026	-.063	.022	-.010	-.119	.147*	-.186**	-.049	.079	.264*	-.090	.239*	1						
SH[15]	.140*	.106	.036	-.025	-.095	.051	-.145*	-.054	-.015	-.024	.013	.183**	-.023	-.092	1					
SV[16]	-.041	-.057	-.006	-.032	-.033	-.049	-.020	-.105	-.157*	.144*	.056	.181**	-.095	-.037	.192**	1				
RA[17]	.062	.057	.026	-.036	-.003	-.013	.028	.084	.048	.019	-.105	-.089	.082	-.012	.237**	.265*	1			
SC[18]	.011	-.008	.069	-.019	.056	-.150*	-.051	-.125	-.059	.184**	.159*	.056	.006	.112	.303**	.355*	.207**	1		
TV[19]	-.001	-.030	.039	-.034	.023	-.039	-.134*	-.032	-.008	.088	-.044	.087	.002	-.074	.230**	.343*	.406**	.332*	1	
CV[20]	.088	.081	-.042	.045	.006	-.034	-.064	.017	.133*	.133*	-.059	-.078	.054	.109	.195**	.187*	.387**	.320*	.439*	1
CC[21]	.052	-.012	.024	.017	.032	.071	.028	-.087	.084	.212**	.017	.024	-.006	.027	.059	.297*	.366**	.310*	.372*	.212**

*Correlation is significant at the 0.05 level (2-tailed)

**Correlation is significant at the 0.01 level (2-tailed)



4.4 Regression Analysis

4.4.1 Corporate Governance Mechanisms and Earnings Management (Model 1)

The following Table 4.7 presents the results of multiple regression analysis for direct effect of corporate governance mechanisms on earnings management specifically discretionary accruals (DA) for the year 2009, 2010 and combination of both years (all year). As illustrated in Table 4.7, only F value for 2009 is statistically significant at 5 percent level with F-value of 2.158 and adjusted R square is 0.105. It informs that the model explained 10.5 percent of the total variance in the earnings management. However, the F value for 2010 and all years are insignificant with adjusted R square of 2.8 and 4.5 percents respectively. The low adjusted R square for each year including all years is consistent with prior empirical studies (Xie *et al.*, 2003; Abdul Rahman and Mohamed Ali, 2006; Ghosh *et al.*, 2010).

TABLE 4.7: Regression Results for Model 1

	Exp Sign	All Year		2009		2010	
		Coefficient	t-stat	Coefficient	t-stat	Coefficient	t-stat
Constant		-0.098	-0.508	-0.478	-1.660	0.383	1.544
BDIND	-	-0.277	-2.697***	-0.292	-2.623**	-0.070	-0.556
BDSZE	-	-0.182	-2.012**	-0.192	-1.609	-0.066	-0.493
CEOD	+	-0.078	-1.132	-0.096	-1.024	-0.047	-0.487
ACIND	-	0.238	2.880***	0.168	1.510	0.221	1.839*
ACEXP	-	0.022	0.314	0.168	1.775*	-0.140	-1.443
INOWN	-	-0.018	-0.257	0.041	0.426	-0.082	-0.811
OUTOWN	-	0.110	0.1627	0.005	0.051	0.242	2.568**
INSTOWN	-	-0.069	-1.025	-0.165	-1.790*	-0.010	-0.103
SIZE	-	0.089	1.106	0.254	2.392**	-0.170	-1.427
LEV	+	-0.090	-1.151	-0.086	-0.835	-0.036	-0.321
ROA	+	0.124	1.689*	0.097	0.987	0.119	1.119
AUDQ	-	-0.059	-0.833	-0.171	-1.817*	0.135	1.323
Adj. R ²		0.028		0.105		0.045	
F-Value		1.575		2.158**		1.470	
N		240		120		120	

Notes:*** and * denote significance at the 1%, 5% and 10% level.

Dependent variable is the mean of discretionary accruals (DA)

Table 4.7 shows the board independence variable (BDIND) is negatively significant at 5 percent level in 2009 and at 1 percent level in all year with β coefficient of -0.292 and -0.277 respectively. Thus, H_{A1} is supported. The results imply that a company with higher board independence is more likely to disclose high quality of financial reporting. It supports the prediction of agency theory and is consistent with most prior studies such as documented by Klein (2002), Davidson *et al.* (2005), Peasnell *et al.* (2005), Hutchinson *et al.* (2008), Jaggi *et al.* (2009) and Lin and Hwang (2010). They concluded that independence of board of directors is the effective monitoring tool for corporate governance in reducing earning management activities. Board size (BDSZE) has significant and negative correlation with earnings management in the pooled data at 5 percent level as expected but insignificant statistical relationship in 2009 and 2010. Regarding the pooled data, H_{A2} is supported. The result indicates that board size has potential to be an effective factor for corporate governance in preventing earnings management activities. In line with previous studies which showed that board size is negatively significant with earnings management (Beasley and Salterio, 2001 and Ghosh *et al.*, 2010) and negatively associated with firm value (Yermack, 1996).



Contradictory to the expectation, it is found that CEO duality (CEOD) has negative relation with earnings management, however its relationship is insignificant in each year and entire year. The result suggests that the combination position of chairman and CEO does not influence the company management to manipulate earnings report. Thus, H_{A3} is not supported. This finding is similar with several Malaysian studies regarding the association between CEO duality and earnings management (Johari *et al.*, 2009), company performance (Abdullah, 2004), financial restatements (Abdullah *et al.* 2010) and financial distress (Abdullah 2006). In other countries, related studies are conducted by Xie *et al.* (2003) and Ghosh *et al.* (2010) who found the combination position of CEO Chairman is unrelated to earnings management.

There is a marginally positively significant relationship between audit committee independence (ACIND) and earnings management at the 10 percent level in 2010 with β coefficient of 0.221 and it is positively significant at 1 percent level in the pooled data with β coefficient of 0.238. The independence audit committee is found to be less efficient in preventing opportunistic behaviour of company management in managing corporate earnings. Direction of the relationship between independence audit committee and earnings management is contradicted with the proposed hypothesis H_{A4} , thus H_{A4} is not supported. The evidence indicates that having a high level of audit committee independence is still unable to reduce earnings management activities the company. In the Malaysian context, this finding is also shared by Abdul Rahman and Mohamed Ali (2006) who reported audit committee independence has insignificant relationship with earnings management due to domination of management over board. In the international context, studies conducted by Baxter and Cotter (2009) and Ghosh *et al.* (2010) also found similar results to this study. Surprisingly, it is found that audit committee expertise (ACEXP) is positively significant with earnings management in each year and all year round. Therefore, H_{A5} is not supported. The result is not impossible to occur in the situation of high enforcement of good corporate governance practices such as in the Malaysian environment since most of the listed companies tend to include qualified accountants as audit committee members in order to comply with the suggestion of MCCG (2007). Implicitly, this qualification is not a guarantee that they are truly independent in accomplishing their responsibility as monitors in the financial reporting process. The finding by Ghosh *et al.* (2010) showed that earnings management for the post-SOX (Sarbanes-Oxley Act) years and pre-SOX years does not vary with the expertise of audit committee.

The relationship between insider ownership (INOWN) and earnings management is not significant for each year and the all year. The results imply that managers as owners have not the potential to reduce manipulation of earnings activities even though the results show a positive sign between insider ownership (INOWN) and earnings management in 2009. In contrast with theoretical expectation, insider ownership which was shown by the high level of average (38%) is unable to deter earnings management activities. This is consistent with a study conducted by Johari *et al.* (2009) who found the company which has ownership by managers more than 25 percent may increase the potential to manage earnings. Furthermore, Hutchinson *et al.* (2008) documented increasing executive shareholdings motivates manager to manage earnings. Therefore, H_{A6} is not supported. Other empirical researches showed insignificant relationship between insider ownership and earnings management. The related studies are done by Ghosh *et al.* (2010), Abdullah *et al.* (2010), Farooq and Jai (2012). Outsider ownership (OUTOWN) shows a positive sign in relation to earnings management. The relationship is insignificant in 2009 and in pooled data but positively significant in 2010 indicating that interest by outside directors do not influence quality of financial reporting. Thus, H_{A7} is not supported. In the Malaysian scenario, the result is not consistent with the study done by Abdullah (2006) who reported non-executive directors' interest is negatively associated with financial distress and Hashim (2009) who found positively significant with earnings quality. The study finds institutional ownership (INSTOWN) is marginally significant with earnings management in 2009 at 10 percent level with β coefficient of -0.165. However, the result is not significant in 2010 and in pooled data. It indicates that institutional investors have potential to be an effective monitor on company management activities, especially in relating to process of reporting earnings. Thus, H_{A8} is marginally supported. The result contradicts with Hadani *et al.* (2011), Velury and Jenkins (2006) and Farooq and Jai (2012). In the Malaysian context, Abdullah *et al.* (2010)



showed outside block holder ownership is effective in preventing firms from misstating accounts and financial distress Abdullah (2006).

4.4.2 Moderating Effects of Recognition and Appreciation (Model 2 and 3)

There are four corporate leader values (at individual level of corporate leader) tested to see whether there is any significant influence on the relationship between corporate governance mechanisms and earnings management. These values are sense of recognition and appreciation (RA), spiritual health (SH), sense of community (SC), and spiritual values (SV). The related hypotheses alternatives to be tested are H_{9A1} to H_{9A3} . Table 4.8 reports the results of hierarchical regression analysis in testing the effect of recognition and appreciation (RA) on the relationship between corporate governance mechanisms and earnings management. It presents multiple regression results for model 2 and 3 specifically in 2009, 2010 and all year (pooled data). Model 2 shows regression analysis of eight independent variables of corporate governance mechanisms; board independence (BDIND), board size (BDSIZE), CEO duality (CEOD), audit committee independence (ACIND), audit committee expertise (ACEXP), insider ownership (INOWN), outsider ownership (OUTOWN) and institutional ownership (INSTOWN) with four control variables namely company size (SIZE), company leverage (LEV), return on assets (ROA) and audit quality (AUDQ). F value in 2010 and all year (pooled data) are not significant but in 2009 it is marginally significant at 10 percent level with value of 1.999. F change in 2009 and all year are not significant while in 2010 it is marginally significant at 10 percent level. Thus, it can be concluded that sense of recognition and appreciation has no direct relationship with earnings management.

Model 3 presents regression analysis of eight independent variables of corporate governance mechanisms, four control variables and eight interaction terms between sense of recognition and appreciation of corporate leader and eight of corporate governance mechanisms. F value for 2009 and all year (pooled data) are significant at 1 percent and 5 percent levels with values of 2.311 and 1.863 respectively. F change for 2009 and all year (pooled data) also significant at 5 percent level with values of 2.459 and 2.330 respectively. The results indicate that sense of recognition and appreciation of corporate leader can influence the relationship between corporate governance mechanisms and earnings management. Two interaction terms have significance association with earnings management in all year and four interaction terms are significant in 2009. The related four independent variables which have significance interaction with recognition and appreciation of corporate leader in 2009 are board independence, audit committee independence, audit committee expertise and insider ownership with β coefficient of 3.059, -2.804, -2.325 and -3.206 respectively. In pooled data, interaction with board independence is significant at 5 percent level and with audit committee expertise is significant at 1 percent level with β coefficients of 2.346 and -2.192 respectively. The results of interaction terms for the above four corporate governance mechanisms can be seen clearly through plotting a graph. Thus, Figure 4.1, Figure 4.2, Figure 4.3 and Figure 4.4 present the graphs of interaction between the two levels of recognition and appreciation of corporate leader (low and high) with two levels of board independence, audit committee independence, audit committee expertise and insider ownership (low and high respectively) and mean of discretionary accruals (earnings management).



TABLE 4.8: Hierarchical Regression Results for Interaction Effects of Recognition and Appreciation (RA) of Corporate Leader on Corporate Governance Mechanisms and Earnings Management

	Exp Sign	All Year				2009				2010			
		Model 2		Model 3		Model 2		Model 3		Model 2		Model 3	
		Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat
Constant		-0.214	-0.898	-0.747	-0.681	-0.379	-1.097	-1.761	-1.080	0.040	0.127	-0.734	-0.519
BDIND	-	-0.228	-2.704***	-2.423	-2.283**	-0.287	-2.558**	-3.106	-2.136**	-0.057	-0.458	-1.036	-0.658
BDSIZE	-	-0.181	-2.003**	-0.832	-0.813	-0.192	-1.597	-1.187	-0.870	-0.058	-0.441	0.734	0.483
CEOD	+	-0.074	-1.082	0.285	0.334	-0.098	-1.047	-0.395	-0.346	-0.034	-0.356	1.091	0.853
ACIND	-	0.239	2.888***	1.607	1.602	0.163	1.453	2.759	1.970*	0.206	1.731*	0.275	0.183
ACEXP	-	0.019	0.270	2.178	2.672***	0.170	1.794*	2.503	2.241**	-0.149	-1.555	2.166	1.840*
INOWN	-	-0.023	-0.323	1.393	1.575	0.047	0.480	3.249	2.391**	-0.092	-0.918	0.291	0.243
OUTOWN	-	0.109	1.597	0.582	0.478	0.005	0.058	-0.517	-0.309	0.234	2.504**	0.922	0.522
INSTOWN	-	-0.073	-1.080	0.180	0.269	-0.162	-1.740*	-0.160	-0.144	-0.022	-0.237	-0.070	-0.073
SIZE	-	0.095	1.175	0.063	0.776	0.251	2.359**	0.154	1.418	-0.144	-1.206	-0.176	-1.413
LEV	+	-0.088	-1.132	-0.074	-0.958	-0.087	-0.843	-0.079	-0.784	-0.033	-0.292	-0.023	-0.200
ROA	+	0.118	1.596	0.107	1.413	0.103	1.039	0.089	0.907	0.101	0.954	0.116	1.027
AUDQ	-	-0.058	-0.822	-0.013	-0.177	-0.174	-1.841*	-0.086	-0.895	0.128	1.269	0.166	1.589
RA		0.054	0.828	0.354	0.619	-0.047	-0.523	0.727	0.908	0.164	1.802*	0.625	0.777
RA*BDIND				2.346	2.057**			3.059	1.923*			1.008	0.606
RA*BDSIZE				0.693	0.647			1.102	0.770			-0.848	-0.535
RA*CEOD				-0.401	-0.467			0.246	0.215			-1.176	-0.914
RA*ACIND				-1.504	-1.341			-2.804	-1.835*			-0.036	-0.021
RA*ACEXP				-2.192	-2.647***			-2.325	-2.064**			-2.386	-1.986*
RA*INOWN				-1.394	-1.545			-3.206	-2.321**			-0.345	-0.282
RA*OUTOWN				-0.465	-0.383			0.517	0.309			-0.677	-0.384
RA*INSTOWN				-0.211	-0.315			0.060	0.054			0.084	0.087
R ²		0.080		0.152		0.197		0.331		0.167		0.231	
Adj. R ²		0.027		0.070		0.098		0.188		0.065		0.067	
R ² Change		0.003		0.072		0.002		0.134		0.026		0.064	
F Change		0.685		2.330**		0.273		2.459**		3.247*		1.024	
F-Value		1.505		1.863**		1.999**		2.311***		1.635		1.404	
Durbin Watson		1.909		1.909		2.123		2.123		2.043		2.043	
N		240		240		120		120		120		120	

Notes: ***, ** and * denote significance at the 1%, 5% and 10% level
Dependent variable is the mean of discretionary accruals (DA)



Moderating effects of RA on BD independence and earnings management

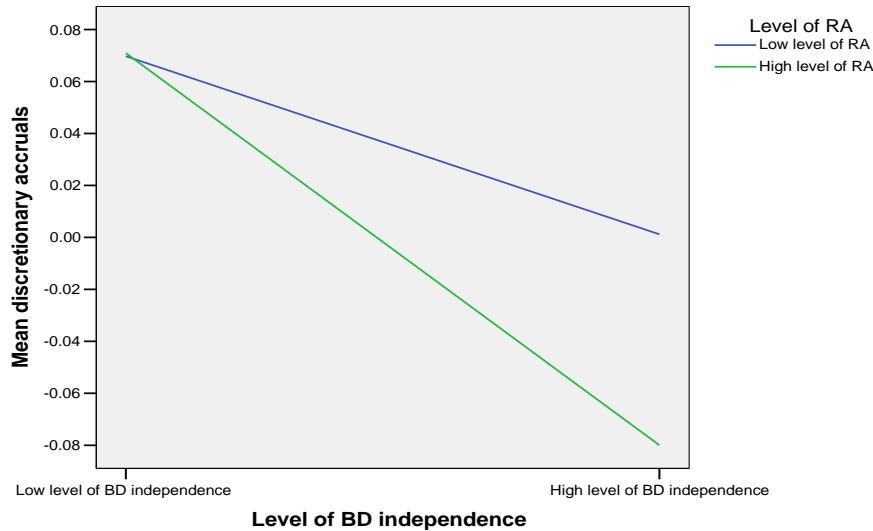


FIGURE 4.1: Moderating effects of recognition and appreciation (RA) on board independence and earnings management (DA)

Figure 4.1 shows the companies which have corporate leaders with high level of recognition and appreciation report low earnings management (high quality of financial reporting). The low level of recognition and appreciation also show similar direction with the high level but its slope is less than the high level of recognition and appreciation of corporate leader. It means that the companies which have corporate leader with low level of recognition and appreciation report high earnings management (low quality of financial reporting) even though it has high level of board independence. Thus, it can be suggested that the sense of recognition and appreciation of corporate leader can influence the relationship between the board independence and financial reporting quality.



Moderating effects of RA on AC independence and earnings management

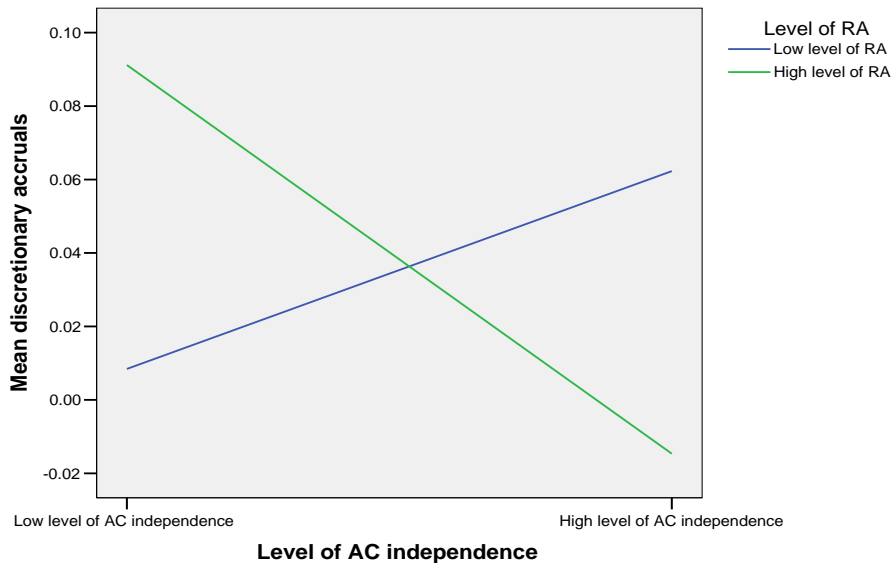


FIGURE 4.2: Moderating effects of recognition and appreciation (RA) on audit committee independence and earnings management (DA)

Figure 4.2 shows the relationship between audit committee independence and discretionary accruals (earnings management) is positively correlated for high level of recognition and appreciation of corporate leader and negatively correlated for low level of recognition and appreciation of corporate leader. It explains that the companies which have corporate leader with high level of recognition and appreciation and high level of audit committee independence report low earnings management (high quality of financial reporting). Meanwhile, the companies which have corporate leader with low level of recognition and appreciation and high level of audit committee independence report high earnings management (low quality of financial reporting). It means that recognition and appreciation of corporate leader can moderate the relationship between audit committee independence and financial reporting quality.



Moderating effects of RA on expertise AC and earnings management

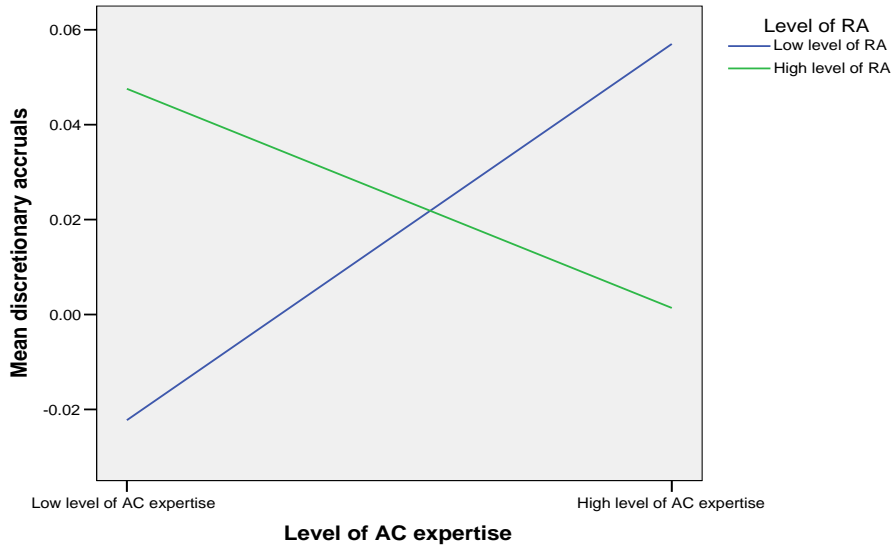


FIGURE 4.3: Moderating effects of recognition and appreciation (RA) on audit committee expertise and earnings management (DA)

Figure 4.3 shows the companies which have high sense of recognition and appreciation of corporate leader and more accountants in audit committee report low earnings management (high quality of financial reporting). The companies which have low sense of recognition and appreciation of corporate leader even though more accountants in audit committees report high earnings management (low quality of financial reporting). The above graph clearly shows that the sense of recognition and appreciation of corporate leader can influence the relationship between expertise of audit committee and financial reporting quality. Therefore, H_{9A3} is supported.



Moderating effects of RA on insider ownership and earnings management

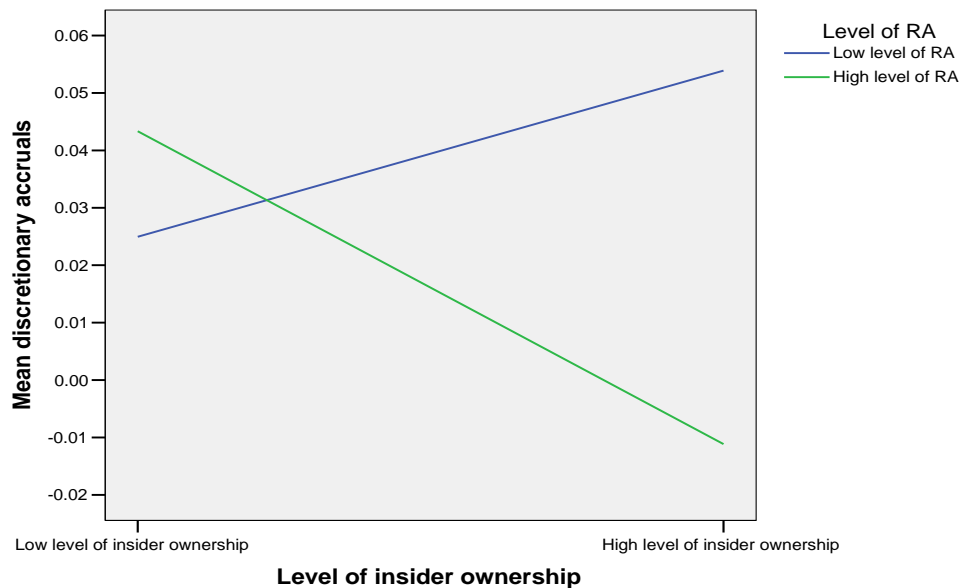


FIGURE 4.4: Moderating effects of recognition and appreciation (RA) on insider ownership and earnings management (DA)

Figure 4.4 shows the companies which have high sense of recognition and appreciation of corporate leader and high insider ownership report low earnings management (high quality of financial reporting). However the companies which have low sense of recognition and appreciation of corporate leader and high insider ownership report high earnings management (low quality of financial reporting). Thus, it is indicated that the sense of recognition and appreciation of corporate leader can moderate the relationship between insider ownership and financial reporting quality.

4.4.3 Moderating Effects of Spiritual Health (SH)

Table 4.9 reports hierarchical regression analysis results for direct effects in model 2 and moderating effects of spiritual health (SH) of corporate leader in model 3 on the relationship between corporate governance mechanisms and earnings management in 2009, 2010 and all year (pooled data). As depicted in model 2, F value in 2010 and all year are significant at 5 percent level with values of 1.898 and 1.838 respectively whereas F change also significant at 5 percent level with values of 6.172 and 5.051 respectively. These results show that sense of spiritual health of corporate leader has positive relationship with earnings management. In model 3, F value in 2009, 2010 and all year (pooled data) are significant at 5 percent level with values of 1.973, 1.684 and 1.896 respectively whereas F change is significant at 10 percent level only in 2009 and all year (pooled data) with values of 1.737 and 1.896. The result reveals that there is a moderating effect of spiritual health in 2009 and in all year. Thus, spiritual health of corporate leader has significant influence on the relationship between insider ownership and earnings management in 2009 but marginally significant at 10 percent level in pooled data on the relationship between board independence, audit committee expertise, insider ownership and earnings management.



TABLE 4.9: Hierarchical Regression Results for Interaction Effects of Spiritual Health (SH) of Corporate Leader on Corporate Governance Mechanisms and Earnings Management

	Exp Sign	All Year				2009				2010			
		Model 2		Model 3		Model 2		Model 3		Model 2		Model 3	
		Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat
Constant		-0.394	-1.696	-0.668	-0.502	-0.582	-1.723	-2.979	-1.638	-0.091	-0.295	1.709	0.862
BDIND	-	-0.221	-2.647***	-2.220	-2.149**	-0.291	-2.605**	-0.668	-0.477	-0.075	-0.615	-3.211	-2.184**
BDSIZE	-	-0.175	-1.947*	-1.039	-0.966	-0.186	-1.541	0.213	0.145	-0.070	-0.538	-1.665	-1.097
CEOD	+	-0.072	-1.052	-0.939	-1.255	-0.093	-0.989	-1.466	-1.347	-0.040	-0.427	-0.671	-0.660
ACIND	-	0.224	2.726***	1.308	1.252	0.165	1.478	1.077	0.787	0.204	1.739*	0.965	0.576
ACEXP	-	0.049	0.710	1.690	1.863*	0.177	1.841*	1.779	1.338	-0.095	-0.988	1.714	1.418
INOWN	-	-0.013	-0.186	1.821	1.764*	0.044	0.449	3.264	2.347**	-0.079	-0.802	-0.375	-0.251
OUTOWN	-	0.112	1.658*	0.944	0.509	0.003	0.031	3.394	1.342	0.250	2.709***	-3.578	-1.335
INSTOWN	-	-0.061	-0.914	0.003	0.003	-0.162	-1.747*	-1.510	-0.928	-0.005	-0.053	0.086	0.058
SIZE	-	0.093	1.158	0.084	1.044	0.249	2.333**	0.209	1.946*	-0.135	-1.152	-0.159	-1.308
LEV	+	-0.132	-1.678*	-0.125	-1.590	-0.095	-0.910	-0.062	-0.596	-0.105	-0.921	-0.131	-1.123
ROA	+	0.110	1.502	0.084	1.124	0.097	0.986	0.075	0.751	0.081	0.772	0.081	0.736
AUDQ	-	-0.046	-0.662	-0.032	-0.464	-0.165	-1.748*	-0.120	-1.273	0.132	1.333	0.126	1.263
SH		0.148	2.247**	0.270	0.406	0.054	0.593	1.231	1.438	0.229	2.484**	-0.742	-0.698
SH*BDIND				2.130	1.936*			0.359	0.240			3.321	2.132**
SH*BDSIZE				0.968	0.856			-0.362	-0.235			1.718	1.069
SH*CEOD				0.851	1.140			1.366	1.264			0.598	0.587
SH*ACIND				-1.215	-1.026			-0.990	-0.644			-0.816	-0.424
SH*ACEXP				-1.608	-1.798*			1.597	-1.215			-1.767	-1.489
SH*INOWN				-1.862	-1.793*			-3.223	-2.311**			0.246	0.163
SH*OUTOWN				-0.827	-0.447			-3.384	-1.341			3.839	1.433
SH*INSTOWN				-0.074	-0.073			1.355	0.833			-0.109	-0.074
R ²		0.096		0.155		0.198		0.297		0.189		0.265	
Adj. R ²		0.044		0.073		0.099		0.147		0.089		0.108	
R ² Change		0.020		0.059		0.003		0.100		0.047		0.076	
F Change		5.051**		1.896*		0.352		1.737*		6.172**		1.273	
F-Value		1.838**		1.896**		2.007		1.973**		1.898**		1.684**	
Durbin Watson		1.871		1.871		2.209		2.209		1.977		1.977	
N		240		240		120		120		120		120	

Notes: ***, ** and * denote significance at the 1%, 5% and 10% level
Dependent variable is the mean of discretionary accruals (DA)



The interaction effects of spiritual health on insider ownership and earnings management can be viewed clearly by plotting graph as presented in Figure 4.5 below.



FIGURE 4.5: Moderating effects of spiritual health (SH) on insider ownership and earnings management (DA)

Figure 4.5 shows the relationship between insider ownership and mean discretionary accruals (earnings management) is negatively correlated for high sense of spiritual health of corporate leader and positively correlated for low sense of spiritual health of corporate leader. In other words, the companies which have high sense of spiritual health of corporate leader and high insider ownership report low earnings management (high quality of financial reporting). In contrast, the companies which have low sense of spiritual health of corporate leader and high insider ownership report high earnings management (low quality of financial reporting). The result reveals that spiritual health of corporate leader has moderating effects on the relationship between insider ownership and earnings management. Therefore, H_{9A1} is supported.

4.4.3 Moderating Effects of Spiritual Values (SV) and Sense of Community (SC)

Table 4.10 and Table 4.11 present hierarchical regression results for sense of spiritual values (SV) and sense of community (SC) of corporate leader for model 2 and model 3 in 2009, 2010 and all year (pooled data). Both factors also categorised as sense of corporate leader values components beside sense of recognition and appreciation (RA) and spiritual health (SH). As illustrated in Table 4.10, F value for model 2 in 2009 is significant at 5 percent level with value of 1.977 but it is not significant in 2010 and all year. While F change in 2009, 2010 and all year (pooled data) are not significant. It suggests that sense of spiritual values of corporate leader has no direct relationship with earnings management. In model 3, F value and F change in each year and all year (pooled data) also not significant. Thus, it can be decided that spiritual values (SV) of corporate leader do not influence the relationship between corporate governance mechanisms and earnings management. In Table 4.11, model 2 shows that only F value in 2009 is significant at 5 percent level with value of 1.973 but it is not significant in 2010 and all year. Whereas F change only shows significant in 2010 at 5 percent level with value of 4.829. It can be concluded that sense of community (SC) of corporate leader has no direct relationship between corporate governance mechanisms and earnings management.



TABLE 4.10: Hierarchical Regression Results for Interaction Effects of Spiritual Values (SV) of Corporate Leader on Corporate Governance Mechanisms and Earnings Management

	Exp Sign	All Year				2009				2010			
		Model 2		Model 3		Model 2		Model 3		Model 2		Model 3	
		<i>Coeff</i>	<i>t-stat</i>	<i>Coeff</i>	<i>t-stat</i>	<i>Coeff</i>	<i>t-stat</i>	<i>Coeff</i>	<i>t-stat</i>	<i>Coeff</i>	<i>t-stat</i>	<i>Coeff</i>	<i>t-stat</i>
Constant		-0.114	-0.490	0.370	0.329	-0.444	-1.299	-1.076	-0.625	0.257	0.844	1.956	1.392
BDIND	-	-0.227	-2.693***	-1.479	-1.410	-0.290	-2.581**	-2.276	-1.542	-0.068	-0.540	-1.028	-0.668
BDSIZE	-	-0.182	-2.010**	-0.203	-0.190	-0.191	-1.587	-0.111	-0.074	-0.065	-0.488	0.055	0.035
CEOD	+	-0.078	-1.129	0.530	0.556	-0.096	-1.021	0.723	0.582	-0.046	-0.474	0.347	0.246
ACIND	-	0.239	2.875***	0.773	0.768	0.166	1.481	2.103	1.466	0.225	1.869*	-0.508	-0.316
ACEXP	-	0.022	0.315	-0.433	-0.439	0.167	1.761*	-0.400	-0.303	-0.139	-1.427	-0.534	-0.368
INOWN	-	-0.018	-0.252	-0.170	-0.162	0.041	0.423	0.979	0.653	-0.079	-0.775	-1.245	-0.869
OUTOWN	-	0.112	1.623	-0.364	-0.529	0.002	0.020	0.876	0.849	0.253	2.644***	-1.971	-2.068**
INSTOWN	-	-0.070	-1.030	0.766	0.808	-0.162	-1.725*	-1.094	-0.875	-0.015	-0.155	1.312	0.902
SIZE	-	0.089	1.105	0.096	1.159	0.253	2.380**	0.260	2.280**	-0.170	-1.418	-0.165	-1.371
LEV	+	-0.091	-1.155	-0.123	-1.514	-0.084	-0.804	-0.096	-0.876	-0.048	-0.415	-0.086	-0.737
ROA	+	0.125	1.689*	0.120	1.520	0.096	0.971	0.075	0.693	0.121	1.127	0.135	1.200
AUDQ	-	-0.058	-0.827	-0.068	-0.941	-0.171*	-1.814*	-0.149	-1.524	0.137	1.343	0.100	0.965
SV		0.008	0.125	-0.247	-0.422	-0.017	-0.187	0.291	0.337	0.068	0.724	-0.882	-1.134
SV*BDIND				1.331	1.189			2.153	1.328			0.972	0.605
SV*BDSIZE				0.023	0.020			-0.057	-0.035			-0.149	-0.092
SV*CEOD				-0.584	-0.611			-0.798	-0.644			-0.383	-0.270
SV*ACIND				-0.566	-0.513			-2.120	-1.348			0.856	0.487
SV*ACEXP				0.459	0.462			0.565	0.427			0.405	0.276
SV*INOWN				0.133	0.128			-0.969	-0.651			1.125	0.792
SV*OUTOWN				0.495	0.733			-0.842	-0.839			2.243	2.389**
SV*INSTOWN				-0.838	-0.878			0.940	0.749			-1.341	-0.915
R ²		0.077		0.096		0.195		0.242		0.146		0.232	
Adj. R ²		0.024		0.009		0.096		0.079		0.041		0.067	
R ² Change		0.000		0.019		0.000		0.046		0.004		0.086	
F Change		0.016		0.587		0.035		0.751		0.524		1.376	
F-Value		1.449		1.108		1.977**		1.487		1.391		1.410	
Durbin Watson		1.808		1.808		2.161		2.161		1.850		1.850	
N		240		240		120		120		120		120	

Notes: ***, ** and * denote significance at the 1%, 5% and 10% level

Dependent variable is the mean of discretionary accruals (DA)



TABLE 4.11: Hierarchical Regression Results for Interaction Effects of Sense of Community (SC) of Corporate Leader on Corporate Governance Mechanisms and Earnings Management

	Exp Sign	All Year				2009				2010			
		Model 2		Model 3		Model 2		Model 3		Model 2		Model 3	
		Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat
Constant		-0.229	-1.054	-1.619	-1.291	-0.476	-1.474	-2.161	-1.036	0.094	0.339	-0.517	-0.331
BDIND	-	-0.245	-2.879***	-0.292	-0.255	-0.292	-2.565**	-0.742	-0.456	-0.114	-0.910	-0.978	-0.575
BDSIZE	-	-0.189	-2.089**	0.572	0.583	-0.192	-1.598	0.712	0.521	-0.085	-0.647	-0.049	-0.032
CEOD	+	-0.086	-1.256	0.905	1.059	-0.095	-1.017	1.868	1.440	-0.076	-0.789	0.145	0.130
ACIND	-	0.259	3.077***	1.102	1.249	0.167	1.477	1.681	1.297	0.274	2.273**	1.530	1.064
ACEXP	-	0.027	0.396	0.476	0.538	0.167	1.759*	0.568	1.025	-0.130	-1.359	-0.071	-0.055
INOWN	-	-0.017	-0.238	-0.325	-0.336	0.041	0.424	-1.537	-0.944	-0.079	-0.800	0.162	0.126
OUTOWN	-	0.116	1.705*	-0.092	-0.163	0.005	0.050	0.699	0.786	0.252	2.715***	-1.057	-1.398
INSTOWN	-	-0.079	-1.173	0.439	0.374	-0.165	-1.758*	-0.597	-0.449	-0.030	-0.317	1.559	0.835
SIZE	-	0.078	0.962	0.067	0.810	0.254	2.369**	0.254	2.318***	-0.197	-1.669*	0.233	-1.915*
LEV	+	-0.094	-1.210	-0.094	-1.157	-0.086	-0.830	-0.117	-1.098	-0.047	-0.424	-0.008	-0.070
ROA	+	0.130	1.761*	0.147	1.958*	0.097	0.981	0.126	1.241	0.136	1.293	0.145	1.335
AUDQ	-	-0.065	-0.929	-0.079	-1.088	-0.171	-1.804*	-0.204	-2.069**	0.116	1.153	0.116	1.114
SC		0.088	1.302	0.873	1.246	-0.001	-0.016	0.896	0.805	0.206	2.198**	0.602	0.639
SC*BDIND				0.036	0.029			0.435	0.241			0.949	0.521
SC*BDSIZE				-0.824	-0.787			-0.992	-0.670			-0.024	-0.015
SC*CEOD				-0.992	-1.148			-1.976	-1.513			-0.189	-0.166
SC*ACIND				-0.886	-0.941			-1.574	-1.135			-1.331	-0.875
SC*ACEXP				-0.445	-0.496			-0.388	-0.680			-0.059	-0.045
SC*INOWN				0.306	0.318			1.573	0.977			-0.262	-0.204
SC*OUTOWN				0.209	0.374			-0.678	-0.774			1.324	1.766*
SC*INSTOWN				-0.514	-0.436			0.479	0.358			-1.599	-0.852
R ²		0.084		0.104		0.195		0.250		0.179		0.222	
Adj. R ²		0.031		0.018		0.096		0.089		0.078		0.056	
R ² Change		0.007		0.021		0.000		0.055		0.037		0.044	
F Change		1.696		0.625		0.000		0.894		4.829**		0.686	
F-Value		1.589*		1.209		1.973**		1.552*		1.777		1.335	
Durbin Watson		1.821		1.821		2.072		2.072		2.053		2.053	
N		240		240		120		120		120		120	

Notes: ***, ** and * denote significance at the 1%, 5% and 10% level
Dependent variable is the mean of discretionary accruals (DA)



In model 3, F value and F change in 2009, 2010 and all year are not significant. Thus, it can be decided that sense of community (SC) of corporate leader do not influence the relationship between corporate governance mechanisms and earnings management.

4.4.4 Moderating Effects of Team Values and Corporate Values on Corporate Governance Mechanisms and Earnings Management

Team Values

As shown in Table 4.12, model 2 shows that F value in 2009 is significant at 5 percent level; however F change is not significant. While F value and F change in 2010 and all year are not significant. Thus, team values have no direct relationship with earnings management. In model 3, F value in each year and all year (pooled data) are not significant. F change also not significant in each year and all year. This result suggests that there is no moderating effect of team values (TV) on the relationship between corporate governance mechanisms and earnings management. Therefore, H_{9A4} is not supported.

Corporate Values

Table 4.13 summarises the hierarchical regression results of corporate values (CV) on the relationship between corporate governance mechanisms and earnings management. In model 2, F value in 2009 and all year are significant at 5 percent and 1 percent levels however F change in each year and all year are not significant. Thus, it suggests that corporate values (CV) have no direct relationship with earnings management. In model 3, F value in 2009 and all year (pooled data) are significant at 1 percent level with values of 2.200 and 2.096. F change for 2009 is significant at 5 percent level but in all year, it is significant at 1 percent level. The results indicated that the corporate values (CV) can influence the relationship between corporate governance mechanisms and earnings management. In other words, corporate values moderate the relationship between audit committee independence and earnings management at 5 percent level in 2009 and in pooled data with β coefficient of -3.067 and -2.556. Interaction between audit committee expertise and corporate values is marginally significant at 10 percent level with β coefficient of -1.637 in pooled data.

Corporate Concern

Model 2 in Table 4.14 shows that only F value in 2009 is significant at 5 percent level with value of 1.987 but it is not significant in 2010 and all year (pooled data). Whereas F change in each year and all year (pooled data) is not significant. Thus, it can be decided that corporate concern (CC) has no direct relationship with earnings management. Model 3 reports F value and F change are not significant in each year and pooled data. This result informs that there is no moderating effect in this model. Thus, it can be concluded that the corporate concern (CC) do not moderate the relationship between corporate governance mechanisms and earnings management.



TABLE 4.12: Hierarchical Regression Results for Interaction Effects of Team Values (TV) of Corporate Leader on Corporate Governance Mechanisms and Earnings Management

	Exp Sign	All Year				2009				2010			
		Model 2		Model 3		Model 2		Model 3		Model 2		Model 3	
		Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat
Constant		-0.161	-0.683	-2.149	-1.876*	-0.551	-1.569	-1.867	-1.091	0.265	0.871	-1.513	-1.011
BDIND	-	-0.229	-2.713***	-0.524	-0.462	-0.298	-2.637**	-1.666	-1.012	-0.067	-0.533	-1.748	-1.058
BDSIZE	-	-0.183	-2.013**	1.171	1.253	-0.194	-1.616	0.604	0.470	-0.063	-0.472	0.805	0.587
CEOD	+	-0.079	-1.152	1.159	1.210	-0.097	-1.030	0.682	0.510	-0.051	-0.524	1.751	1.306
ACIND	-	0.240	2.891***	1.291	1.248	0.172	1.536	1.944	1.334	0.218	1.805*	2.335	1.535
ACEXP	-	0.026	0.374	0.463	0.515	0.173	1.803*	0.200	0.164	-0.132	-1.355	0.757	0.583
INOWN	-	-0.018	-0.258	0.114	0.130	0.039	0.402	-0.347	-0.248	-0.079	-0.777	-0.506	-0.438
OUTOWN	-	0.111	1.626	-0.023	-0.029	0.006	0.067	-0.140	-0.124	0.241	2.547**	0.487	0.461
INSTOWN	-	-0.072	-1.059	0.882	1.085	-0.171	-1.819*	-1.159	-1.006	-0.012	-0.131	1.388	1.131
SIZE	-	0.092	1.134	0.085	1.018	0.257	2.404**	0.297	2.561**	-0.166	-1.383	-0.177	-1.444
LEV	+	-0.094	-1.201	-0.126	1.538	-0.092	-0.876	-0.140	-1.259	-0.045	-0.394	-0.092	-0.766
ROA	+	0.122	1.656*	0.131	1.713*	0.095	0.961	0.112	1.075	0.114	1.066	0.114	1.015
AUDQ	-	-0.057	-0.814	-0.055	-0.761	-0.169*	-1.791*	-0.155	-1.568	0.137	1.344	0.155	1.463
TV		0.031	0.466	1.100	1.812*	0.034	0.364	0.639	0.727	0.061	0.671	1.099	1.302
TV*BDIND				0.301	0.248			1.481	0.819			1.753	1.009
TV*BDSIZE				-1.444	-1.476			-0.825	-0.613			-0.939	-0.650
TV*CEOD				-1.217	-1.267			-0.756	-0.564			-1.775	-1.318
TV*ACIND				-1.143	-1.004			-1.889	-1.204			-2.370	-1.377
TV*ACEXP				-0.452	-0.504			-0.040	-0.033			-0.898	-0.687
TV*INOWN				-0.119	-0.135			0.393	0.278			0.443	0.384
TV*OUTOWN				0.129	0.166			0.126	0.111			-0.235	-0.223
TV*INSTOWN				-0.969	-1.191			0.935	0.816			-1.395	-1.137
R ²		0.078		0.111		0.196		0.234		0.145		0.212	
Adj. R ²		0.025		0.025		0.097		0.070		0.040		0.043	
R ² Change		0.001		0.033		0.001		0.038		0.004		0.067	
F Change		0.217		1.008		0.133		0.609		0.450		1.041	
F-Value		1.466		1.292		1.986**		1.425		1.385		1.257	
Durbin Watson		1.823		1.823		2.168		2.168		1.998		1.998	
N		240		240		120		120		120		120	

Notes: ***, ** and * denote significance at the 1%, 5% and 10% level
Dependent variable is the mean of discretionary accruals (DA)



TABLE 4.13: Hierarchical Regression Results for Interaction Effects of Corporate Values (CV) of Corporate Leader on Corporate Governance Mechanisms and Earnings Management

	Exp Sign	All Year				2009				2010			
		Model 2		Model 3		Model 2		Model 3		Model 2		Model 3	
		Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat
Constant		-0.324	-1.313	-2.974	-2.555**	-0.653	-1.842*	-4.269	-2.256**	0.119	0.359	-2.166	-1.511
BDIND	-	-0.222	-2.644***	-1.624	-1.479	-0.296	-2.654***	-2.050	-1.382	-0.054	-0.426	-0.958	-0.559
BDSIZE	-	-0.183	-2.025**	0.212	0.183	-0.193	-1.615	1.459	0.832	-0.066	-0.501	0.729	0.444
CEOD	+	-0.078	-1.135	0.741	0.736	-0.094	-1.003	1.206	0.876	-0.048	-0.497	0.414	0.278
ACIND	-	0.235	2.844***	2.586	2.602**	0.172	1.541	3.069	2.223**	0.207	1.721*	1.641	1.087
ACEXP	-	0.028	0.411	1.631	1.667*	0.172	1.819*	1.887	1.457	-0.131	-1.346	1.221	0.830
INOWN	-	-0.020	-0.288	1.665	1.601	0.038	0.391	1.039	0.664	-0.083	-0.825	2.199	1.548
OUTOWN	-	0.097	1.420	0.283	0.305	-0.003	-0.028	-0.174	-0.130	0.223	2.338**	0.366	0.284
INSTOWN	-	-0.085	-1.246	-0.241	-0.116	-0.180	-1.912*	-2.840	-1.189	-0.028	-0.291	2.925	0.804
SIZE	-	0.101	1.253	0.095	1.198	0.257	2.423**	0.243	2.317**	-0.147	-1.214	-0.155	-1.250
LEV	+	-0.088	-1.131	-0.078	-0.974	-0.082	-0.790	-0.096	-0.909	-0.040	-0.350	-0.026	-0.212
ROA	+	0.120	1.634	0.086	1.190	0.094	0.957	0.089	0.925	0.111	1.043	0.055	0.502
AUDQ	-	-0.072	-1.017	-0.019	-0.262	-0.177	-1.875*	-0.109	-1.117	0.112	1.079	0.160	1.452
CV		0.096	1.461	1.375	2.485**	0.076	0.848	1.731	2.027**	0.114	1.199	1.309	1.779*
CV*BDIND				1.449	1.284			1.851	1.173			0.924	0.538
CV*BDSIZE				-0.414	-0.333			-1.719	-0.915			-0.860	-0.490
CV*CEOD				-0.806	-0.798			-1.277	-0.926			-0.449	-0.299
CV*ACIND				-2.556	-2.366**			-3.067	-2.083**			-1.581	-0.948
CV*ACEXP				-1.637	-1.660*			-1.770	-1.365			-1.387	-0.930
CV*INOWN				-1.723	-1.647			-1.050	-0.669			-2.330	-1.628
CV*OUTOWN				-0.185	-0.197			0.147	0.109			-0.111	-0.086
CV*INSTOWN				0.155	0.074			2.676	1.121			-2.967	-0.816
R ²		0.086		0.168		0.200		0.320		0.153		0.229	
Adj. R ²		0.033		0.088		0.102		0.175		0.049		0.064	
R ² Change		0.009		0.082		0.005		0.120		0.011		0.076	
F Change		2.134		2.701***		0.720		2.164**		1.439		1.212	
F-Value		1.626*		2.096***		2.042**		2.200***		1.473		1.388	
Durbin Watson		1.972		1.972		2.197		2.197		2.133		2.133	
N		240		240		120		120		120		120	

Notes: ***, ** and * denote significance at the 1%, 5% and 10% level
Dependent variable is the mean of discretionary accruals (DA)



TABLE 4.14: Hierarchical Regression Results for Interaction Effects of Corporate Concern (CC) of Corporate Leader on Corporate Governance Mechanisms and Earnings Management

	Exp Sign	All Year				2009				2010			
		Model 2		Model 3		Model 2		Model 3		Model 2		Model 3	
		Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat	Coeff	t-stat
Constant		-0.209	-0.897	-0.996	-0.775	-0.407	-1.172	-0.534	-0.280	0.053	0.179	-1.019	-0.592
BDIND	-	-0.224	-2.652***	-0.476	-0.361	-0.294	-2.629**	-1.669	-0.919	-0.061	-0.492	-0.187	-0.097
BDSIZE	-	-0.179	-1.968*	-0.667	-0.553	-0.196	-1.629	-1.262	-0.758	-0.064	-0.484	-0.692	-0.390
CEOD	+	-0.080	-1.164	1.076	1.197	-0.095	-1.009	1.527	1.214	-0.055	-0.578	0.042	0.032
ACIND	-	0.230	2.761***	1.560	1.458	0.173	1.539	2.337	1.585	0.197	1.650	1.259	0.795
ACEXP	-	0.022	0.315	0.363	0.330	0.166	1.753*	-0.330	-0.222	-0.146	-1.527	1.598	0.984
INOWN	-	-0.014	-0.189	-0.932	-0.874	0.038	0.395	-0.930	-0.540	-0.066	-0.658	-0.279	-0.194
OUTOWN	-	0.103	1.512	0.591	0.631	0.010	0.101	0.853	0.667	0.224	2.389**	0.464	0.338
INSTOWN	-	-0.081	-1.179	-0.187	-0.160	-0.157	-1.647	-1.259	-0.904	-0.047	-0.497	1.316	0.714
SIZE	-	0.091	1.129	0.110	1.315	0.252	2.372**	0.269	2.372**	-0.161	-1.363	-0.144	-1.157
LEV	+	-0.089	-1.144	-0.114	-1.371	-0.087	-0.838	-0.119	-1.073	-0.037	-0.328	-0.021	-0.169
ROA	+	0.124	1.687*	0.136	1.789*	0.097	0.985	0.110	1.057	0.119	1.132	0.128	1.152
AUDQ	-	-0.060	-0.855	-0.062	-0.860	-0.170	-1.805*	-0.161	-1.658	0.127	1.260	0.122	1.176
CC		0.056	0.851	0.441	0.676	-0.034	-0.372	0.002	0.002	0.181	1.973*	0.758	0.808
CC*BDIND				0.267	0.189			1.494	0.757			0.151	0.074
CC*BDSIZE				0.497	0.389			1.128	0.641			0.661	0.351
CC*CEOD				-1.164	-1.268			-1.654	-1.290			-0.046	-0.035
CC*ACIND				-1.511	-1.227			-2.479	-1.466			-1.233	-0.672
CC*ACEXP				-0.356	-0.318			0.490	0.325			-1.805	-1.086
CC*INOWN				0.931	0.873			0.995	0.577			0.220	0.153
CC*OUTOWN				-0.492	-0.521			-0.874	-0.673			-0.229	-0.167
CC*INSTOWN				0.139	0.117			1.165	0.823			-1.379	-0.739
R ²		0.080		0.101		0.196		0.226		0.172		0.200	
Adj. R ²		0.027		0.014		0.097		0.061		0.070		0.029	
R ² Change		0.003		0.021		0.001		0.031		0.030		0.028	
F Change		0.725		0.643		0.138		0.484		3.894*		0.432	
F-Value		1.508		1.167		1.987**		1.366		1.693**		1.168	
Durbin Watson		1.792		1.792		2.081		2.081		1.958		1.958	
N		240		240		120		120		120		120	

Notes: ***, ** and * denote significance at the 1%, 5% and 10% level
Dependent variable is the mean of discretionary accruals (DA)

The following Figure 4.6 plots a graph to show the interaction effects between corporate values and audit committee independence on earnings management.

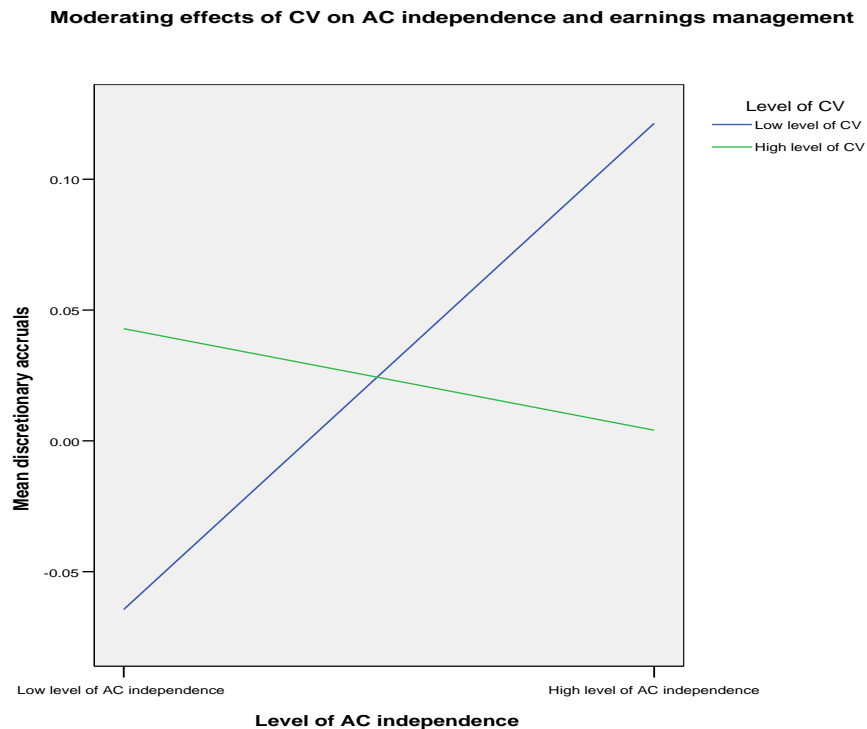


FIGURE 4.6: Moderating effects of corporate values (CV) on audit committee independence and earnings management (DA)

As illustrated in Figure 4.6, the company with high corporate values and high level of audit committee independence reports low earnings management (high quality of financial reporting). On the other hand, the company with low corporate values and low audit committee independence reports high earnings management (low quality of financial reporting). This graph suggests the corporate values moderate the relationship between audit committee independence and earnings management. Therefore, H_{9A5} is supported.

5. DISCUSSION AND CONCLUSION

5.1 Discussion

At individual level, only sense of recognition and appreciation and sense of spiritual health show a significant relationship on corporate governance mechanisms and financial reporting quality. At team and corporate level, only corporate values influence the relationship of corporate governance mechanisms and financial reporting quality.

5.1.1 Sense of Recognition and Appreciation of Corporate Leader

The study finds that the sense of recognition and appreciation of corporate leader moderates the relationship between corporate governance mechanisms, especially board independence, audit committee expertise, insider



ownership and earnings management. These results indicate that the corporate leaders who have a high sense of working together, sense of belonging to workplace community and deep feeling of being connected tend to serve the best for corporation and stakeholder interest. These corporate leaders are motivated to give full support and cooperation to independent directors as well as executive directors (manager) in monitoring and preparing the corporate financial report. Not surprisingly, it may provide a high possibility for company to disclose high quality of financial reporting. Most prior studies provides evidence regarding the corporate leader who has a high sense of recognition and appreciation tends to develop higher organisational commitment (Milliman *et al.*, 2003; Duchon and Plowman, 2005; Rego and Cunha, 2008; Pawar 2009; Fry *et al.* 2011).

Recognition and appreciation is explained as a deeper sense of connection among people which includes freedom of expression, support and caring (Milliman *et al.*, 2003), sense of being connected to others (Giacalone and Jurkiewicz, 2003), the notions of sharing, mutual obligation and commitment (Duchon and Plowman, 2005) and an experience of interconnectedness among those involved in a work process (Marques, 2006). The related items contained in recognition and appreciation factor are 'we work together to resolve conflict in a positive way', 'I feel I am valued as a person in my job' and 'I feel that I am a part of a community in my immediate workplace'. These items explain the sense of recognition and appreciation of corporate leader as working together towards organisation interest, they feel part of workplace community (inside community) and feel connected to community (outside community). The deep sense of values increases sense of attachment, loyalty and effectiveness to an organisation and result in better contribution of corporate leader to the corporation (Rego and Cunha, 2008; Pawar, 2009). As the role model for a corporation, the commitment of the corporate leader is more likely to share his/her values and bring together his/her subordinates to serve for the best interest of all stakeholders, whether inside or outside communities.

5.1.2 Sense of Spiritual Health of Corporate Leader

Secondly, sense of spiritual health of corporate leader influences the relationship between corporate governance mechanisms (insider ownership) and earnings management. It suggests that the corporate leader who has a high deep sense of spirituality has more potential to influence his/her subordinates to have integrity, to be honesty and have sense of humility in managing the corporation. The success of a corporate leader begins with personal integrity and honesty and is then transformed in good behaviour such as ethical commitment (Reave, 2005). Consequently, these values help the corporate leader make ethical decision making for the future interest of corporation and outside community. He also tends to give more cooperation and support to company management, including the executive director, to be more objective and transparent in making decisions in those activities which relate to preparing and disclosing financial reporting. This is consistent with the findings by Choi and Pae (2011) who found that companies with a high level of ethical commitment are more likely to report high quality of financial reporting (less engaged in earnings management) and be more conservative in reporting of earnings.

The spiritual health factor is explained as nourishment to inner life of corporate leader by Ashmos and Duchon (2000), as feelings of completeness and joy by Giacalone and Jurkiewicz (2003) and as personal goodwill by Marques (2006). For the purpose of the study, there are two items contained in spiritual health, namely 'I consider myself a spiritual person' and 'I care about the spiritual health of my subordinates'. Both items inform that the sense of spirituality of a corporate leader and his/her subordinates are important to create spiritual health at the workplace. The result suggests that sense of spiritual health of corporate leader is an intrinsic motivation to top management to be honest and have integrity in managing and controlling the corporation. This principle corporate leader has high potential to influence other managers, including executive director (manager also as director), to be effective in overseeing the financial reporting process.

Prior empirical research documented that the spiritual health of a corporate leader is positively related with intrinsic, extrinsic and work rewards satisfaction (Kolodinsky *et al.*, 2007), physical and mental health as well as



job satisfaction (Sprung *et al.*, 2012) and higher work productivity (Garcia-Zamor, 2003). They suggest that managers as well as administrators in both private and public sectors can use workplace spirituality to improve performance and create an ethical organisation. Daniel (2010) supported that an organisation which encouraged workplace spirituality tends to have team effectiveness in terms of trust, creativity and respect. The current study by Fry *et al.* (2011) revealed that spiritual well-being (calling and membership) mediates the relationship between spiritual leadership with the organisational performance and commitment. Since most corporate failures and scandals are caused by top management, the spiritual health of a corporate leader is crucial to be nourished through establishing spirituality at the workplace (McCuddy and Pirie, 2007).

5.1.3 Corporate Values

Corporate values is strongly significant as a moderating factor to the relationship between corporate governance mechanisms (audit committee independence) and earnings management in discretionary accruals (DA) model in 2009 and in pooled data. It means that the sense of corporate values will enhance the effective role of audit committee in mitigating earnings management activities. In this context, the finding of the study informs that the company with a higher sense of corporate values tends to provide full support and cooperation to independent directors in audit committee to meet their responsibility in overseeing the process of financial reporting. As the prominent factor to company management, the corporate values should be implemented in the workplace by the corporate leader and other corporate members for the health and sustainability of their corporation. Similar as other factors of workplace spirituality, corporate values items are adapted from organisation values components as suggested by Ashmos and Duchon (2000) and Milliman *et al.* (2003). However, the study is only concerned with several items that are categorised as corporate values such as 'this corporation encourages the creation of community', 'this corporation has conscience', 'the corporation I work for cares about whether my spirit is energised by my work', and 'I feel positive about my future with this corporation'. These four items explain the overall sense of corporate values among Malaysian corporations from the top corporate leaders' views. Corporate values and strongly principled corporate leaders integrate each other to be a crucial role in promoting employee work attitudes (Milliman *et al.* 2003), organisational commitment and organisational performance (Fry, 2003; Duchon and Plowman, 2005). It can be suggested that the sense of corporate values is also a potential factor to the company in preparing and presenting high integrity of financial reporting.

5.2 Conclusion

The study concentrates on the role and influence of corporate leader values on corporate governance mechanisms and earnings management among Malaysian listed companies. The corporate leaders selected in the study are Chief Executive Officers (CEOs) or Managing Directors (MDs) as they are the most influential leader in a corporation. Experiences of corporate scandals and failures in both developed and developing countries reveal that majority of the cases involved are corporate leaders, especially Chief Executive Officers (CEOs), Chief Financial Officers (CFOs) and corporate directors. In addition, past corporate governance studies are inconclusive to suggest the efficiency of existing corporate governance mechanisms in enhancing quality of financial reporting. Most researchers (Zohar and Marshall, 2004; Reave, 2005; Arfah and Aziuddin, 2008) argue that the intellectual of corporate leader and corporate governance mechanism are not enough to sustain the corporation in future. The corporate leader should have another ability to be an effective leader. The study argues that corporate leader value is very important to improve quality corporate governance and financial reporting. This research gap is strongly supported by spiritual leadership theory, workplace spirituality, stewardship theory, and human governance concept.

The study reveals that the Malaysian corporate leaders' values as measured by workplace spirituality are still at low to moderate level across religion and ethnicity. It's suggesting that the Malaysian corporate leaders have a



moderate sense of human values. There is some conscience with regard to spirituality but it is not widely practiced. In other words, Malaysian corporate leaders still do not have a strong sense of integrity, honesty and ethical in working environment. Therefore, Malaysian corporate governance needs a paradigm shift on thinking among corporate leaders because quality of corporate governance cannot be improved if only the model or structure of corporate governance is improved. Sense of spirituality at the individual level among corporate people especially corporate leader is important factor in order to promote workplace spirituality. These results suggest that whilst spirituality is given a place in the heart of Malaysian corporate leaders, wide spirituality practices is yet to be given due attention and focus.

Most interestingly, the study suggests a supplemented approach to corporate governance system to be more effective in preventing earnings management activities. The study reveals that corporate leader value (value based approach) is the important factor to strengthen the function of corporate governance in the financial reporting process. These corporate leaders are the strongly principled or ethical corporate leader. In the context of Malaysian corporations, the significant corporate leader value is sense of recognition and appreciation. It shows that sense of belonging to the workplace community, sense of working together in achieving the corporate goals, being valued and appreciated by the organisation and sense of connection to outside community is important among Malaysian corporate leaders. This value presents about corporate leaders' relationship with workplace community and society or known as horizontal relationship. The second important value to Malaysian corporate leaders is sense of spiritual health. It expresses about sense of spiritual well-being of corporate leader and their subordinates. This value explains about the strength of corporate leaders' relationship with Creator or known as vertical relationship. Both values are interconnectedness in energising sense of integrity, honesty and ethical among corporate leader and corporate members in organising and governing corporation. Consequently, sense of recognition and appreciation and sense of spiritual health of corporate leader can influence corporate governance mechanisms especially board independence, audit committee expertise and insider ownership to be more efficient in mitigating earnings management.

Spiritual leadership theory, workplace spirituality, stewardship theory, and human governance concept consistently agreed that a deep sense of spirituality among corporate leaders is the strong foundation to develop workplace spirituality or value based corporate culture. Sense of spirituality is initiated from a deep layer in human self of corporate leader. It has interconnectedness with emotional and thinking system. Thus, when a corporate leader has a deep sense of vision, meaning and value, it will touch his emotional and then shifted his thinking paradigm to change his attributes, behaviour and attitudes to be more integrity and ethical (Zohar, 1997). Findings of study shows the importance role of corporate leader values in shaping a value based corporate culture, enhancing quality of corporate governance system and then improving quality of corporate financial reporting. This healthy corporate culture is the most conducive environment for business organisation since it is developed based on trust and integrity among corporate people. The corporate leader and corporate members are motivated to serve the best for others than serve for themselves.

The value based governance is found to be the best internal solution to corporate governance system and it becomes a supplemented approach to corporate governance mechanisms which already has a strong structure (external solution) as proposed by good corporate governance principles. The role of corporate leader value is very important to activate sense of spirituality in corporate governance in creating value based governance. It likes a soul to corporate governance mechanisms to energise a healthy function of corporate governance system. Thus, the role of integrity or ethical corporate leader and corporate governance structure are interconnectedness in developing a strong corporate governance system. The function and contribution of corporate management and corporate owners are important to ensure the successful and sustainability of corporation. Hence, both parties cannot be viewed as separate entity as proposed by the agency theory. The human governance concept which has a similar basis as spirituality leadership theory, workplace spirituality theory and stewardship theory seen corporate management (CEO) and corporate owners as interconnectedness parties in building learning organisation which



can contribute benefits to stakeholders and the whole society. Therefore, it is important to suggest that the human governance concept should be integrated with corporate governance mechanisms in order to build a strong function of corporate governance system in mitigating opportunistic behaviour or unethical actions among corporate people especially in manipulation of earnings reports.

References:

- Abdullah, S. N. (2006). Board structure and ownership in Malaysia: the case of distressed listed companies. *Corporate Governance: International Journal of Business in Society*, 6(5), 582–594.
- Abdullah, G. A., Alzaidiyeen, N. J. and Aldarabah, I. T. (2009). Workplace spirituality and leadership effectiveness among educational managers in Malaysia. *European Journal of Social Sciences*, 10(2), 304-316.
- Abdul Rahman, R. and Ali, F. H. M. (2006). Board, audit committee, culture and earnings management: Malaysian evidence. *Managerial Auditing Journal*, 21(7), 783-804.
- Abdul Wahab, E. A., How, J. C. Y. and Verhoeven, P. (2007). The impact of the Malaysian Code on Corporate Governance: compliance, institutional investors and stock performance. *Journal of Contemporary Accounting & Economics*, 3(2), 106 – 129.
- Al-Attas, S. M. N. (1995). *Prolegomena to the Metaphysics of Islam: An Exposition of the Fundamental Elements of the Worldview of Islam*. International Institute of Islamic Thought and Civilization (ISTAC), KL.
- Al-Jamal of Fez, S.A. as translated by Abd as-Rahman at-Tarjumana, A. (1977). *The meaning of man-the foundation of the science of knowledge*. England: Diwan Press.
- Al-Mahdi, M. (2004). *On Being Khalifah of Allah*. The Khalifah Institute, Selangor: Malaysia.
- Arfah, S and Aziuddin, A. (2008). *Human Governance: A paradigm shift in governing corporations*. MPH Group Publishing Sdn. Bhd. Petaling Jaya: Malaysia.
- Ashmos, D.P. and Duchon, D. (2000). Spirituality at work: A conceptualization and measure. *Journal of Management Inquiry*, 9(2), 134-145.
- Baker, T., Collins, D. and Reitenga, A. (2000). Stock option compensation and earnings management incentives. *Journal of Accounting, Auditing & Finance*, 557-582.
- Baxter, P., and Cotter, J. (2009). Audit committees and earnings quality. *Accounting and Finance*, 49, 267-290.
- Bliss, M. A., Gul, F. A. and Majid, A. (2011). Do political connections affect the role of independent audit committees and CEO Duality? Some evidence from Malaysian audit pricing. *Journal of Contemporary Accounting & Economics*, 82–98.
- Bursa Malaysia (BM). 2001. Audited annual reports at <http://www.bm.com>. December 2010.
- Covey, S. R. (1995). Principle-centered leadership – sharpen the saw. Retrieved on 16 May 2008 from <http://www.qualitydigest.com/nov95/html/prin-cnt.html>.



- Daniel, J. L. (2010). The effect of workplace spirituality on team effectiveness. *Journal of Management Development*, 29(5), 442–456.
- Davidson, R., Goodwin, J. and Kent, P. (2005). Internal governance structures and earnings management. *Accounting and Finance*, 45, 241-267.
- Davis, J. H., Schoorman, F. D. and Donaldson, L. (1997). Toward a stewardship theory of management. *The Academy of Management Review*, 22(1), 20-47.
- DeAngelo, L. E. (1981). Auditor size and audit quality. *Journal of Accounting and Economics*, 3, 183-199.
- Dechow, P. M., Sloan, R. G. and Sweeney, A. P. (1995). Detecting earnings management, *The Accounting Review*, 70, 193–225.
- DeZoort, F. T. and Salterio, S. E. (2001). The effects of corporate governance experience and financial-reporting and audit knowledge on audit committee members' judgments. *AUDITING: A Journal of Practice & Theory*, 20(2), 31–47.
- Donaldson, L. and Davis, J. H. (1991). Stewardship theory or agency theory: CEO governance and shareholder returns. *Australian Journal of Management*, 16(1), 50-64.
- Duchon, D. and Plowman, D. A. (2005). Nurturing the spirit at work: impact on work unit performance. *The Leadership Quarterly*, 16, 807–833.
- Efendi, J., Srivastava, A. and Swanson, E. P. (2007). Why do corporate managers misstate financial statements? The role of option compensation and other factors. *Journal of Financial Economics*, 85, 667-708.
- Fry, L. W. (2003). Toward a theory of spiritual leadership. *The Leadership Quarterly*, 14, 693-727.
- Fry, L. W., Hannah, S. T., Noel, M. and Walumbwa, F. O. (2011). Impact of spiritual leadership on unit performance. *The Leadership Quarterly*, 22, 259–270.
- Garcia-Zamor, Jean-Claude. (2003). Workplace spirituality and organizational performance. *Public Administration Review*, 63(3), 355–363.
- Ghosh, A., Marra, A. and Moon, D. (2010). Corporate boards, audit committees, and earnings management: pre- and post-SOX evidence. *Journal of Business Finance & Accounting*, 37(9&10), 1145–1176.
- Giacalone, R. A. and Jurkiewicz, C. L. (2003). Toward a science of workplace spirituality. In R. A. Giacalone & C.L. Jurkiewicz (Eds.) *Handbook of workplace spirituality and organizational performance* (pp. 3–38), New York: M.E. Sharp.
- Gujarati, D. N. and Porter, D. C. (2009). *Basic econometrics*, 5th edition. McGrawHill: Singapore.
- Gul, F. A. (2006). Auditors' response to political connections and cronyism in Malaysia. *Journal of Accounting Research*, 44(5), 931-963.



- Hadani, M., Garanova, M., and Khan, R. (2011). Institutional investors, shareholder activism, and earnings management. *Journal of Business Research*, doi:101016/j.jbusres.2010.12.004.
- Hair, J. F., Black, W. C., Babin, B. J. and Anderson, R. E. (2010). *Multivariate data analysis: A global perspective*. 7th Edition. New Jersey: Pearson Education.
- Haque, A. and Mohamed, Y. (2009). *Psychology of personality: Islamic perspectives*. Cengage Learning Asia Pte Ltd: Malaysia.
- Hashim, H. A. (2009). Board of directors, ownership structure, ethnicity and earnings quality: Malaysian Evidence. PhD Thesis. Faculty of Business and Accountancy, University Malaya: Kuala Lumpur.
- Hutchinson, M. R., Percy, M. and Erkurtoglu, L. (2008). An investigation of the association between corporate governance, earnings management and the effect of governance reforms. *Accounting Research Journal*, 21(3), 239–262.
- Jaggi, B., Leung, S., and Gul, F. (2009). Family control, board independence and earning management: Evidence based on Hong Kong firms. *Journal of Accounting and Public Policy*, (28), 281-300.
- Johnson, S. and Mitton, T. (2003). Cronyism and capital controls: evidence from Malaysia. *Journal of Financial Economics*, 67, 351-382.
- Jones, J. (1991). Earnings management during import relief investigations. *Journal of Accounting Research*, 29, 193–228.
- Karakas, F. (2009). Spirituality and performance in organizations: a literature review. *Journal of Business Ethics*, 94, 89–106.
- Klein, A. (2002). Audit committee, board of director characteristics, and earnings management. *Journal of Accounting and Economics*, 33, 375-400.
- Kolodinsky, R. W., Giacalone, R. A. and Jurkiewicz, C. L. (2007). Workplace values and outcomes: exploring personal, organizational, and interactive workplace spirituality. *Journal of Business Ethics*, 81, 465–480.
- Lin, J. W., and Hwang, M. I. (2010). Audit quality, corporate governance, and earnings management: a meta-analysis. *International Journal of Auditing*, 14, 57-77.
- Marques, J. F. (2006). The spiritual workers. *Journal of Management Development*, 25(9), 884–895.
- Marques, J. F. (2008). The spirituality@work protocol. *Human Resource Management International Digest*, 16(2), 3–7.
- McCuddy, M. K. and Pirie, W. L. (2007). Spirituality, stewardship, and financial decision-making: toward a theory of intertemporal stewardship. *Managerial Finance*, 33(12), 957–969.



- Mehra, M. (2005). Corporate Governance: An Alternative Model from chapter 1 in *Reforming Corporate Governance in Southeast Asia: Economics, Politics and Regulations*. Institute of Southeast Asian Studies (ISEAS), Singapore.
- Milliman, J., Czaplewski, A. J and Ferguson, J. (2003). Workplace spirituality and employee work attitudes. *Journal of Organizational Change Management*, 16(4), 426-447.
- Mohd Ali, S., Mohd Salleh, N. and Hassan, M. S. (2008). Ownership structure and earnings management in Malaysian listed companies: the size effect. *Asian Journal of Business and Accounting*, 1(2), 89-116.
- Norman, M. S., Takiah, M. I., and Mohid, M. R (2005). Earning management and board characteristics: evidence from Malaysia. *Jurnal Pengurusan*, 24, 77-103.
- Pawar, B. S. (2009). Individual spirituality, workplace spirituality and work attitudes: an empirical test of direct and interaction effects. *Leadership & Organization Development Journal*, 30(8), 759-777.
- Quatro, S. A., Waldman, D. A. and Galvin, B. M. (2007). Developing holistic leaders: four domains for leadership development and practice. *Human Resource Management Review*, 17, 427-441.
- Reave, L. (2005). Spiritual values and practices related to leadership effectiveness. *The Leadership Quarterly*, 16, 655-687.
- Rego, A. and Cunha, M. P. (2008). Workplace spirituality and organizational commitment: an empirical study. *Journal of Organizational Change Management*, 21(1), 53-75.
- Securities Commission (2007). *The Malaysian code of corporate governance* (Revised 2007). Kuala Lumpur: SC.
- Siregar, S. V. and Utama, S. (2008). Type of earnings management and the effect of ownership structure, firm size, and corporate governance practices: evidence from Indonesia. *The International Journal of Accounting*, 43, 1-27.
- Sprung, J. M., Sliter, M. T. And Jex, S. M. (2012). Spirituality as moderator of the relationship between workplace aggression and employee outcomes. *Personality and Individual Differences*, 1-5.
- Staubus, G. J. (2005). Ethics failures in corporate financial reporting. *Journal of Business Ethics*, 57, 5-15.
- Taib, Fauziah Md. (2009). Accounting scandals and failure of corporate governance: science discovery as a solution? Inaugural Professorial Lecture, No. 1, School of Management, USM: Penang.
- Yermack, D. (1996). Higher market valuation of companies with a small board of directors. *Journal of Financial Economics*, 40, 185-212.
- Zohar, D. (1997). *Rewiring the corporate brain: using the new science to rethink how we structure and lead organization*. San Francisco: Berrett-Koehler Publishers.
- Zohar, D. and Marshall, I. (2004). *Spiritual capital: wealth we can live by*. San Francisco: Berrett-Koehler Publishers.



THE RELATIONSHIP BETWEEN LEADERSHIP BEHAVIOR TO ORGANIZATIONS COMMITMENT, BUDGETARY PARTICIPATION, AND JOB SATISFACTION IN CREATING GOOD GOVERNMENT IN BENGKULU CITY

Iqbal Miftakhul Mujtahid
Indonesia Open University
Muhammad Sil
Indonesia Open University
Isma Coryanata
University of Bengkulu

Email: ismacoryanata@yahoo.com

Abstract

This study purposed to examine the relationship between leadership behavior toward organizations commitment, budgetary participation and job satisfaction. The results of this study were (1) leadership behavior has a positive and significant relationship to organizational commitment in creating a good government, (2) leadership behavior has a positive and significant relationship to the budget participation in creating good government, and (3) leadership behaviors have a positive relationship and significant impact on job satisfaction in creating good government. This study advice (1) effective leadership behaviors can encourage employees are committed to change and instill a new strategy to mobilize and focus the energy and resources of the organization, (2) leadership behavior that open and humanists will make subordinates to communicate that they need, and (3) trustworthy leadership behavior, foster enthusiasm and creativity of his subordinates in order to bring the organization in accordance with the mission and vision in achieving organizational goals.

Keywords: leadership behavior, organizational commitment, budgetary participation, job satisfaction, good government

I. Introduction

The emphasis of research on the behaviors that employees acted outside their official roles (extra role behavior), is a critical factor for the effectiveness of the organization (Morrison and Phelps, 1999). The focus of this study is interesting, because employee behavior is very big role in order to improve organizational performance, but still relatively neglected in empirical research, especially in government agencies where required by the public good government.



Research in the field of leadership has also resulted in the conclusion that leadership behavior affects the perceived job satisfaction of employees. (Vanderberg and Lance, 1992). Job satisfaction is determined by the difference between one's all to be expected with all of the job perceived above all actually received.

From the above discussion, the researcher would like to see more deeply how the relationship between leadership behavior to good government.

1.1. Problem Formulation

Based on the above problems can be formulated as follows:

1. How is the relationship between leadership behaviors on organizational commitment in order to establish good government in the city of Bengkulu.
2. How is the relationship between leadership behavior towards budgetary participation in order to create good government in Bengkulu city government.
3. How is the relationship between leadership behavior on job satisfaction in order to establish good government in the city of Bengkulu.

1.2. Research Objectives

Objectives to be achieved in this study is to assess:

1. Relationship between leadership behavior on organizational commitment in order to establish good government in the city of Bengkulu.
2. Relationship between leadership behavior towards budgetary participation in order to create good government in the city of Bengkulu.
3. Relationship between leadership behavior on job satisfaction in order to establish good government in the city of Bengkulu.

1.3. Benefits of Research

Benefits that will be achieved in this study are:

1. As the material for the evaluation of government officers in organizational commitment, budgetary participation and job satisfaction in creating good government.



2. To add to the depth of knowledge, especially in the field of human resource management and public sector accounting.

II. Literature Review

2.1. Leadership

Pawar and Eastman (1997) defines leadership as a process to achieve a collective goal, through the unification of motives mutual owned by the leader and subordinates. Empirical testing conducted by Howell and Avolio (1993), who concluded that leadership behavior directly and positively affect the performance of the business unit level. Jung and Avolio (2000), found that leadership has both a direct and indirect relationship with the subordinate's performance.

2.2. Organizational Commitment

Commitment to the organization is generally defined as the extent of one's involvement in the organization and strength of identification with a particular organization. Organizational commitment can be characterized by: a) a strong belief against the organization, and acceptance of the goals and values of the organization; b) a willingness to exert effort for the sake of the organization; and c) a strong desire to maintain a relationship with the organization (Meyer et al, 1993). According Arini (2010), in supporting the welfare and success of the organization where she worked someone who has a high commitment to the organization will exhibit the following two characteristics: (1) a strong urge to remain a member of the organization, (2) willingness to do our best for the sake of organization.

2.3. Budgetary Participation

The budget prepared by involving subordinates are more likely to negotiate with your boss about the budget targets may be achieved (Brownell and McInnes, 1986). Some researchers identified that the performance impact of budgetary participation is influenced by psychological factors, such as motivation, locus of control and attitude (attitude), and is also influenced by organizational factors, such as the level of decentralization and leadership style and environmental factors. Characteristics of the budget is needed to menentukan receipt of a budget by budgetees.



The study examined the relationship of participation in budget management performance, showing results that are not always consistent. Indriantoro study (1995) found significantly increased management performance will increase if the budget participation. Research conducted Supomo (1998), showed that participation type has no significant relationship with managerial performance.

2.4. Job Satisfaction

Most research in the field of employee job satisfaction is based on two basic assumptions. First, job satisfaction is a potential determinant to predict absentee rates, displacement, performance and behavior outside of work. Secondly, that the main antecedent employee attitudes can be influenced by the ability of the management company. Empirical evidence presents a conclusion that a person's job satisfaction positively affects organizational commitment. Clugston (2000) found that job satisfaction positively influences affective commitment, continuants, and normative. However, Hackett et al (1994) found that job satisfaction is negatively affecting continuants commitment, and positively associated with affective and normative commitment.

2.5. Relations Leadership Behavior on Organizational Commitment, Budgetary Participation, and Job Satisfaction

Podsakoff et al (1996) concluded that in order to foster the commitment of the members of the organization to change, can be done by applying transformational leadership. Accordingly research also Judge and Bono (2000) and Bycio et al (1995), concluded a significant relationship between transformational leadership behaviors with organizational commitment. A perceived job satisfaction tends to affect the level of commitment to the organization for which he works. Clugston (2000) found that job satisfaction positively influences affective commitment, continuants, and normative. Thus the hypothesis being tested, are:

Hypothesis 1: Behavioral leadership is positively related to organizational commitment in creating good government

Procedural justice is on a leader have a good relationship with managerial performance is indirect through an intervening variable that budgetary participation and procedural fairness have a relationship with job satisfaction, and are directly or indirectly through intervening variables budgetary participation. Thus the two hypotheses are:

Hypothesis 2: The behavior of the leadership is positively related to budget participation in creating good government.

Various research on leadership has resulted in the conclusion that the behavior of the leader was significantly related to the behavior and response of the followers (Podsakoff et al, 1996). Judge and Bono (2000), found that leadership behavior affects job satisfaction and satisfaction of subordinates to leaders. Therefore, three hypotheses to be tested are:

Hypothesis 3: Behavior of leadership is positively related to job satisfaction of subordinates in creating good government.

The frame of mind in this study as follows.

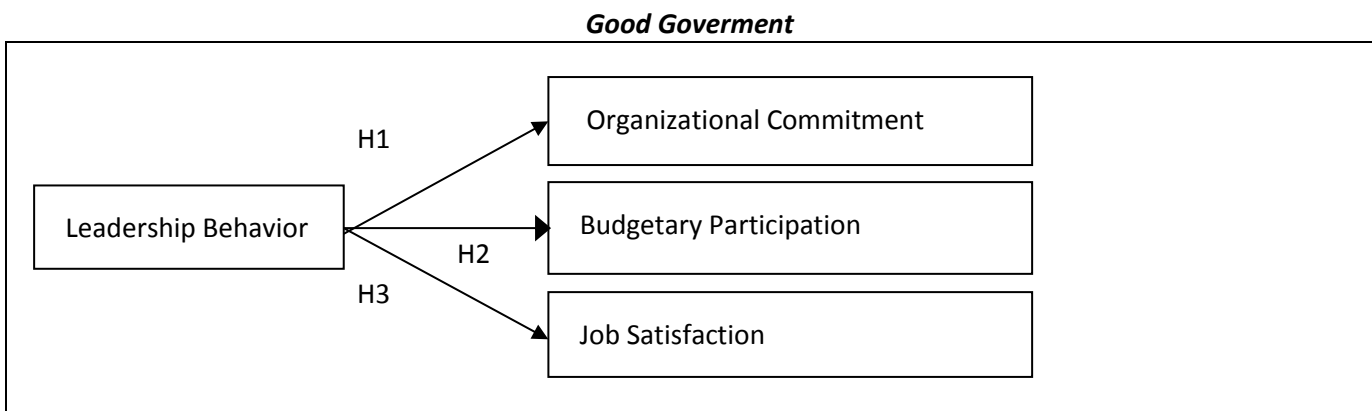


Figure 1. Relations Leadership Behavior on Organizational Commitment, Budgetary Participation, and Job Satisfaction in Creating Good Government.

III. Methodology Research

3.1. Research Approach

This research uses a survey approach and a pilot test of the instrument conducted research on graduate student M. Hum, M.Si, MM, MPP and M Ed in the city of Bengkulu as many as 40 people were taken by purposive sampling method.

3.2. Population and Sampling Method

The study population was the state apparatus in Bengkulu city government in 15 departments, 8 weight, 4 offices on education, and 9 sub-district office. The sampling method using purposive sampling method



with the criteria section heads/fields/section/agency involved in the preparation of the budget of at least 1 year. The number of samples amounted to 86 people.

3.3. Data Collection Method

Means of data collection in this study was done by questionnaire. Questionnaires distributed to each of the state apparatus in Bengkulu city government agencies.

3.4. Methods of Data Analysis

Descriptive statistics were used to summarize the respondents' demographic conditions and a description of the study variables. Hypothesis testing using Spearman correlation analysis.

IV. Results And Discussion

4.1. Description of Data

The distribution of questionnaires administered and delivered directly by the researcher to the respondents who are in departments, agencies, offices, and government districts in the city of Bengkulu listed in Table 4.1 below.

Table 4.1. Distribution of Questionnaire Research in Bengkulu City Government Agencies

No.	Agencies	Total Number of Questionnaires	Questionnaires were Distributed Processing
I	Department:		
	1. Department of Education	5	4
	2. Department of Health	3	3
	3. Department of Cooperatives and Small and Medium Enterprises Development	5	3
	4. Department of Industry and Trade	4	4
	5. Department of Tourism and Culture	3	1
	6. Department of Labor, Youth and Sports	3	2
	7. Departement of Social	4	3
	8. Department of Agriculture and Livestock	4	3
	9. Department of Marine and Fisheries	5	3
	10. Department of Civil Registration	4	4
	11. Departement of Parks and Hygiene	3	2



	12. Department of Transportation, Communication and Information	4	3
	13. Department of Public Works	5	3
	14. Departement of City Planning and Building Supervisor	2	2
	15. Department of Revenue, Finance and Asset Management	3	3
II	Board:		
	1. Inspectorate	4	3
	2. Regional Development Planning Board	4	3
	3. National Unity, Politics and Public Protection Board	3	3
	4. Community Empowerment, Women and Family Planning Board	2	1
	5. Environment Board	3	3
	6. Regional Employment Board	3	2
	7. Food Security and Implementing Guidance Board	3	3
	8. Integrated Licensing Service Board	3	3
III	Office:		
	1. Office of Libraries, Archives and Documentation	3	3
	2. Office of Liaison	3	3
	3. Office of the Civil Service Police Unit	2	1
	4. Fire Department	2	2
IV	Districts:		
	1. Gading Cempaka	1	1
	2. Singaran Pati	2	2
	3. Kampung Melayu	1	1
	4. Muara Bangkahulu	2	2
	5. Ratu Agung	2	2
	6. Ratu Samban	1	1
	7. Selebar	1	1
	8. Sungai Serut	1	1
	9. Teluk Segara	2	2
Total		105	86

Sources: Primary data, processed, 2012

4.2. Description of Respondents

Demographics of the respondents in this study as follows:

Table 4.2. Description of Respondents in Bengkulu City Government Agencies



No	Criteria	Number (people)	Percentage (%)
1	Gender:		
	○ Male	70	81
	○ Female	16	19
2	Age:		
	○ 20 – 30 years old	8	9
	○ 31 – 40 years old	35	41
	○ 41 – 50 years old	28	33
	○ 51 – 60 years old	15	17
3	Education:		
	○ Senior High School	0	0
	○ Bachelor	8	9
	○ Undergraduate	62	72
	○ Postgraduate	16	19
4	Future Work with the office now:		
	○ <1 years	0	0
	○ 1 – 2 years	5	6
	○ 3 – 5 years	21	24
	○ 6 – 8 years	26	30
	○ > 8 years	34	40
5	Position:		
	○ Head Field/Section	59	69
	○ Head Sub-Field/Section	27	31

Sources: Primary data, processed, 2012

Based on Table 4.2 are generally the male respondents are more than the women. Judging from the age, the majority of respondents were in the age range 31-50 years were 63 people, or 74 percent. The education level of respondents, mostly undergraduate (S1) of 62 people or 72 percent. Experience working respondents during his tenure in the City of Bengkulu in over 6 years as many as 60 or 70 percent. Based on his post, respondents generally occupying the position of head field/sections as much as 59 or 69 percent.

4.3. Respondents Perceptions on Organizational Commitment Variables

Persepsi respondents' organizational commitment variables as follows:

Table 4.3 Perceptions of Respondents on Organizational Commitment Variables in Bengkulu City Government Agencies



Scale Likert	Perception	Frequency	Percentage
1.	Strongly Disagree	38	5.52
2.	Disagree	63	9.16
3.	Neutral	130	18.89
4.	Agree	244	35.47
5.	Strongly Agree	213	30.96
	Total	688**	100.00

**86 respondents x 8 statement item = 688

Most respondents agreed and strongly agreed with the frequency of 457 or 66.43 percent committee desirous trying with all effort to help us be successful office, received nearly every type of job assignment in order to keep working in this office, proudly told other people that I work in this office, and this office gives the best opportunities to improve the performance of this office.

Statement of the respondents strongly disagree, disagree, and neutral with 231 or 33.57 percent frequency that is proud of our office as a good organization to work, find the option to work in this office is very precise compared to other offices that have been considered before, and very big awareness of the future of this office.

4.4. Respondents Perceptions on Budgetary Participation Variables

Persepsi respondents to a variable budget participation as follows.

Table 4.4 Perceptions of Respondents on Budgetary Participation Variables in Bengkulu City Government Agencies

Scale Likert	Perception	Frequency	Percentage
1.	Strongly Involved	28	5.43
2.	Not Involved	68	13.18
3.	Neutral	134	25.96
4.	Involved	176	34.11
5.	Highly Engaged	110	21.32
	Total	516**	100.00

**86 respondents x 6 statement item = 516

Sources: Primary data, processed, 2012

Most of the respondents are involved and very engaged with the frequency of 286 or 55.43 percent said the effect input during the last budget, whether the reasons given in the budget revisions are



made, and involvement in the preparation of the budget. Statement respondents sometimes with frequency of 134 or 25.96 percent of the input is given to the importance of budgets and often give opinions/suggestions on the budget at the boss without being asked. Statement respondents strongly involved and not involved with the frequency of 96 or 18.61 percent, which is often asked by the boss to give opinions/suggestions on the budget.

4.5. Respondents Perceptions on Job Satisfaction Variables

Persepsi respondents' job satisfaction variables as follows.

Table 4.5 Perceptions of Respondents on Job Satisfaction Variables in Bengkulu City Government Agencies

Scale Likert	Perception	Frequency	Percentage
1.	Strongly Disagree	45	6.54
2.	Disagree	88	12.79
3.	Neutral	170	24.71
4.	Agree	240	34.88
5.	Strong Agree	145	21.08
	Total	688**	100.00

**86 responden x 8 statement item = 688

Most respondents strongly agree and agree with the frequency of 385 or 55.96 per cent expressed the personality according to the field of work, salary/wages in accordance with the workload, and are satisfied with the salary/wages received. Statement of neutral respondents with frequency 170 or 24.71 percent, which supports the work of the working environment and work according to skills/disciplines. Statement of the respondents strongly disagree and disagree with the frequency of 133 or 19.33 percent, which has the opportunity to develop creativity/ideas in the work, satisfied to have co-workers who can work with, and personality in accordance with the field work.

4.6. Respondents Perceptions on Leadership Behavior Variables

Persepsi subordinates to superiors on leadership behavior variables as follows.

Table 4.6 Perceptions of Respondents on Leadership Behavior Variables in Bengkulu City Government Agencies



Scale Likert	Perception	Frequency	Percentage
1.	Strongly Disagree	11	2.56
2.	Disagree	19	4.42
3.	Neutral	101	23.49
4.	Agree	178	41.39
5.	Strong Agree	121	28.14
	Total	430**	100.00

**86 respondents x 5 statement item = 430.

4.7. Hypothesis Testing

The results of data processing research to determine the relationship of leadership behavior with each of the study variables: organizational commitment, budgetary participation and job satisfaction by using a computer program SPSS version 16 can be seen in Table 4.7 below.

Table 4.7. Hypothesis Test Results Using Spearman Rank Correlation

			COMITMENT_	PARTISIPATION_	JOB_	BEHAVIOR
Spearman's rho	COMITMEN_ ORGANISATION	Correlation	1.000	.608***	.563***	.767***
		Sig. (1-tailed)	.	.000	.000	.000
		N	86	86	86	86
	BUDGET PARTISIPATION_	Correlation	.608***	1.000	.506***	.637***
		Sig. (1-tailed)	.000	.	.000	.000
		N	86	86	86	86
	JOB SATISFACTION	Correlation	.563***	.506***	1.000	.616***
		Sig. (1-tailed)	.000	.000	.	.000
		N	86	86	86	86
	LEADERSHIP BEHAVIOR	Correlation	.767***	.637***	.616***	1.000
		Sig. (1-tailed)	.000	.000	.000	.
		N	86	86	86	86

**. Correlation is significant at the 0.01 level (1-tailed).

Based on the hypothesis test results in Table 4.7, the correlation coefficient between the variables of leadership behavior and organizational commitment has a significance level of 0.767. The relationship between leadership behavior variables were tested with organizational commitment is positive.



Probability value of 0.000 (one-tailed) < standard alpha value of 0.01 means that there is a significant relationship between leadership behavior and organizational commitment.

The coefficient of correlation between leadership behavior variables with budgetary participation has a significance level of 0.637. The relationship between leadership behavior variables with budgetary participation under test is positive. Probability value of 0.000 (one-tailed) < standard alpha value of 0.01 means that there is a significant relationship between leadership behavior with budgetary participation.

The correlation coefficient between the variables of leadership behavior with job satisfaction has a significance level of 0.616. The relationship between the variables of leadership behavior with job satisfaction were tested positive value. Probability value of 0.000 (one-tailed) < standard alpha value of 0.01 means that there is a significant relationship between leadership behavior and job satisfaction.

The magnitude of the relationship between the variables of leadership behavior and organizational commitment, budgetary participation and job satisfaction as follows:

Table 4.8. The Amount of Variable Interpersonal Research on Public Authorities Bengkulu City

No.	Variable	Leadership Behavior	Rate Relationship
		Spearman Correlation	
1.	Organizational Commitment	0.767	Strong
2.	Budget Participation	0.637	Strong
3.	Job Satisfaction	0.616	Strong

Sources: Primary data, processed, 2012

Based on the above table 4.8 Spearman correlation coefficient of 0.767 means that the level of the relationship between leadership behavior and organizational commitment is strong. Spearman correlation coefficient of 0.637 means that the strength of the relationship between leadership behavior level with the participation of the budget, and the Spearman correlation coefficient of 0.616 means that the strength of the relationship between the level of leadership behavior with job satisfaction in Bengkulu city government agencies.

V. Conclusions and Recommendations

5.1. Conclusion

Based on the results of the study can be summarized as follows:



1. Behavior leadership has a positive and strong relationship and significant to the organization's commitment to creating a good government in the city of Bengkulu.
2. Behavior leadership has a positive and strong relationship and significant budgetary participation in creating good government in the city of Bengkulu.
3. Behavior leadership has a positive relationship and a strong and significant impact on job satisfaction in creating good government in the city of Bengkulu.

5.2. Suggestion

1. Conduct effective leadership can encourage employees are committed to change and instill a new strategy to mobilize and focus the energy and resources of the organization.
2. Behavior leadership open and humanists will make them subordinate to communicate the need and responsibility to create a budget.
3. Behavior leadership to trust and to foster enthusiasm and creativity of his subordinates in order to bring the organization in accordance with the mission and vision in achieving organizational goals.

VI. References

- Arini., Eti. , 2010. Affect Job Characteristics and Work Experience on Employee Organizational Commitment Inspectorate Office of Bengkulu province. *Media Economics*, Vol IX No.. 01.
- Brownell, P. and McInnes, M. 1986. Budgetary Participation, Motivation and Managerial Performance, *The Accounting Review*, Vol. . LXI, No.. 4.
- Bycio, P., Hackett, RD and Allen, JS 1995. Further Assessments of Bass's (1985) conceptualisation of Transformational Leadership. *Journal of Applied Psychology*.
- Clugston, M., 2000. The mediating Effects of Multidimensional Commitment on Job Satisfaction and Intent to Leave. *Journal of Organizational Behavior*.
- Hackett, R. D., Bycio, P. and Hausdorf, P.A. , 1994. Assessment of Further Meyer and Allen (1991) Three Components of Organizational Comminent. *Journal of Applied Psychology*.
- Howell, JM, and Avolio, BJ 1993. Transformational Leadership, Transactional Leadership, Locus of Control, and Support for Innovation: Key Predictors of Consolidated-Business-Unit Performance. *Journal of Applied Psychology*.
- Indriantoro, Nur. , 1995. *Accounting Development in Indonesia: The Effects of participative budgetting on Job Performance and Job Satisfaction with Locus of Control and Culture as Moderating Variabels*



Dimensions. Jakarta: Coordinating Team Development Accounting, LPFEUI.

Judge, TA, and Bono, JE, 2000. Five-Factor Model of Personality and Transformational Leadership. *Journal of Applied Psychology*.

Jung, DL, and Avolio, BJ 2000. Opening the Black Box: an Experimental Investigation of the mediating Effects of Trust and Value congruence on Transformational and Transactional Leadership. *Journal of Organizational Behavior*.

Meyer, JP, Allen, NJ, and Smith, CA 1993. Commitment to the Organization and Occupations: Extension and Test of a Three-Component conceptualization. *Journal of Applied psycholog.*

Morrison, EW, and Phelps, CC 1999. Taking Charge at Work: Role Extra Efforts to Initiate Work Place Change. *Academy of Management Journal*.

Pawar, BS, and Eastman, KK 1997., The Nature and Implications of Contextual Influences on Transformational Leadership: A Conceptual Examination. *Academy of Management Review*.

Podsakoff, PM, MacKenzie, SB, and Bommer, WH 1996. Transformational Leader Behaviors and Substitutes for Leaderships Determinants of Employee Satisfaction Commitment, Trust, and Organizational Citizenship Behaviors. *Journal of Management*.

Supomo, Bambang. , 1998. *Influence Of Organizational Structure and Culture Efektifitas Participatory Budget in Managerial Performance Improvement: An Empirical Study on Manufacturing Company in Indonesia.* Yogyakarta: Gadjah Mada University, Thesis.

Vanderberg, RJ, and Lance, CE 1992. Examining the Causal Order of Job Satisfaction and Organizational Commitment. *Journal of Management*.



Audit Fees: The Role of Auditor Type and Audit Market Competition

FAKHRODDIN MOHAMMADREZAEI ^{a*} AND NORMAN MOHD-SALEH ^b

Faculty of Economics and Management,
Universiti Kebangsaan Malaysia, 43600 Bangi, Selangor Darul Ehsan, MALAYSIA
^a fakhroddinmohammadrezaei@yahoo.com, ^b norman@ukm.edu.my

Abstract

In Iran, the audit market liberalization process has resulted in both state and private auditors simultaneously providing audit services and increased competition among these providers. Although numerous studies exist concerning the effect of increased concentration in audit market of developed countries and variety types of auditors on audit fees, the present study contributes to audit fees literature by studying the effect of auditor type (private vs. state) and increased competition in the Iranian audit market on audit fees. Data from firms listed on the Tehran Stock Exchange between 2001 and 2010 are utilized to test the research hypotheses. The findings, after controlling for auditor choice, reveals that private auditors charge lower audit fees in their highly competitive audit market than those of state auditors in their monopolistic market share. Additionally, the results indicate that audit fees decrease as competition increases in the Iranian audit market. The findings suggest that monopolistic power provides an opportunity for a supplier to set prices, which are usually higher than prices in a competitive market. Moreover, the results suggest that the negative effect of weak demand for high quality audit services on audit fees can be exacerbated by increased competition in audit market.

Keywords: private and state auditors, audit market competition, audit fees, market power, Iran

1. INTRODUCTION

Audit market structure (competition or concentration) is among the most controversial topics for both policy makers and researchers following the mergers of the Big audit firms and the scandal of Arthur Andersen. One of the main concerns of policymakers (e.g., European Commission) is that increased concentration in an audit market is likely to increase the market power of Big audit firms. As a result, the audit firms are likely to charge higher audit fees without any improvement in the quality of audit services provided by the auditors. Although the majority of extant studies, in context of developed countries, find that competition (concentration) in an audit market is negatively (positively) associated with audit fees (e.g., Bandyopadhyay and Kao, 2001; Jensen and Payne, 2005; McMeeking, 2007; Ding and Jia, 2012; Carson et al., 2012), Pearson and Trompeter (1994) and Iyer and Iyer (1996) provide evidence that contradicts the conclusions generally reached in extant literature. The findings of Chen et al. (2007) in China show that the fee premiums of the Big audit firms are due to market power rather than reputation. Chen et al. (2007) highlights the importance of audit market circumstances, particularly in regards to whether or not demand for high quality audit services exists. As a result of the conclusion reached regarding the importance of demand for high quality audit services and the fact that extant studies primarily examine audit markets in developed countries, the effect of audit market structure on audit fees in developing countries should be examined.² The negative effect of increased competition in such audit market on audit fees is likely to be more significant than that in audit markets of developed countries.

* Corresponding author

² The argument can be made that the environmental features of developing countries are unfavorable and significantly different from those of developed countries. Karampinis and Hevas (2011) define an 'unfavorable environment' as one characterized by "code-law tradition, bank



In Iran, as a developing country, audit market liberalization resulted in increased competition in audit market and the operation of both private and state auditors simultaneously. Audit market liberalization occurred in late 2001 following the establishment of the Iranian Association of Certified Public Accountants (IACPA). Prior to audit market liberalization, the Iranian Audit Organization (IAO), as state auditor, dominated the Iranian audit market. Following the audit market liberalization, a large number of private audit firms were established and became members of the IACPA, which resulted in intense competition among private auditors. However, although the IAO has lost a part of its market share following audit market liberalization, the IAO still maintains a monopolistic market share over state owned enterprises (SOEs) (see, Bagherpour et al., 2008).

While audit market liberalization is an important public policy issue, only anecdotal evidence exists regarding the implications of the phenomenon (e.g., Bozorg Asl, 2010; Hovansian Far, 2010b). Wrongful competition among private auditors regarding audit fees is among the most controversial topics in the contemporary audit market of Iran (e.g., Bozorg Asl, 2010). Competition among auditors increased dramatically where there is weak demand for high quality audit services. Hence, it is important to determine how increased competition in an unfavorable market affects the pricing strategies of auditors. The objective of the present study is to investigate the effect of auditor type (private vs. state) and audit market competition on audit fees in Iran.

In an effort to hypothesize the effect of auditor type and audit market competition on audit fees, the 'market power' view is applied. Monopolistic situations provide the opportunity for suppliers to set prices, which are usually higher than prices in a competitive market (e.g., Kahana and Katz, 1990; Langbien and Willson, 1994; Mises, 1998). Along similar lines, the majority of extant studies find that increased competition (concentration) in audit market results in low (high) audit fees (e.g., Bandyopadhyay and Koa, 2001; Jensen and Payne, 2005; Ding and Jia, 2012; Carson et al., 2012). The market power of private auditors in their competitive audit market is more likely to be lower than that of the state auditor in his monopolized portion of the audit market. Hence, compared with the state auditor, private auditors charge lower audit fees (first hypothesis). Additionally, following audit market liberalization, not only competition continuously increased among private auditors, but also the monopoly market share of the state auditor significantly decreased. Put differently, competition in audit firm level (market share of each auditor) increased (decreased) continuously following audit market liberalization, which can result in less market power. Therefore, it is expected that audit fees decreases as competition increases in the Iranian audit market (second hypothesis).

The hypotheses of the present study are tested by analyzing all firms (except financial firms) with available data listed on Tehran Stock Exchange (TSE) during the period between 2001 and 2010. Since the disclosure of audit fees is not mandatory, the final sample contains 1,208 firm-year-observations. The first hypothesis is tested by comparing the audit fees of private and state auditors. The second hypothesis is tested by analyzing the effect of competition in audit firm level on audit fees. The results support both research hypotheses. Self-selection bias regarding auditor choice is controlled and several robustness and additional tests are conducted to corroborate the main findings.

The present research contributes to extant accounting literature in several ways. The present study enriches knowledge at the international level regarding the audit profession in Iran by providing detailed information on the developments and changes in the profession. Additionally, accounting literature can be enriched by examining the effective factors on audit fees in the Iranian audit market as an interesting research setting. The Iranian audit market possesses some features that make it as a valuable setting in which to examine audit pricing. Two different audit markets exist in Iran simultaneously: (i) the portion of the audit market monopolized by the state auditor in relation to SOEs; and (ii) the portion of the audit market open for competition among private auditors. Non-audit fees relating to business and governance systems in Iran are not common. The research setting can increase the validity of findings "because joint fee decisions and possible cross-subsidization could severely reduce the reliability of the

orientation, concentrated corporate ownership, poor shareholders' protection, and low regulatory quality" (Karampinis and Hevas, 2011, p. 304). Such features are more likely to result in low demand for high quality audit services. Thus, auditors are less likely to be able to obtain market power by quality differentiation in such environments.



audit fee data that are used” (Chen et al., 2007, p. 5). Iranian audit firms commonly operate only in a local audit market and do not have offices in other cities. Hence, the premise that dominant audit firms at the national level are dominant within in a specific local market is unsupported. However, most previous studies face difficulties with this premise in other countries when regional heterogeneity exists (Bandyopadhyay and Kao, 2004; Chen et al., 2007). Since Iranian auditors have not formed any evident industry specialization, the test setting is more reliable than the settings that are utilized in extant studies in other countries where the impact of industry specialization mixes with that of pricing strategies.

Although prior studies investigate audit fees in regards to a variety of auditor types, such as Big vs. non-Big auditors (e.g., Chen et al., 2007) and industry specialist auditors vs. non-specialist auditors (e.g., Scott and Gist, 2013), the present study expands upon existing accounting literature by comparing the effect of the emergence of private audit practices *vis-à-vis* the use of state auditors in relation to audit fees. There is no consensus among prior studies regarding the main driver (market power or reputation) of Big audit firms’ fee premium. However, the findings of the present study widen the narrow body of knowledge regarding that fee premium of auditors in developing countries can be mainly attributed to market power of the auditor rather than auditor’s reputation (see, Chen et al., 2007). This is the case because auditors in developing countries, due to weak demand for high quality audit services, are less likely to be able to earn fee premium by quality differentiation (reputation).

While Azizkhani et al. (2012) examines audit pricing strategies in Iran, the present study differs from Azizkhani et al. in several ways. The present research explicitly controls for auditor selection bias, whereas Azizkhani et al. ignores the issue. Although Azizkhani et al. study the influence of increased competition in an audit market as a consequence of audit market liberalization on audit fees, such analysis is not performed in the present study because no comparability exists between disclosed audit fees before and after audit market liberalization.³ In addition, such comparing may result in misleading results due to the hyperinflationary economy of Iran. To deal with these problems, the present study investigates the effect of audit market share of each auditor in each year (yearly competition in audit firm level) on audit fees following audit market liberalization. Azizkhani et al. compare audit fees between the state and private auditors and attributes the market power of the state auditor to the auditor’s size. However, the present study argues that the market power of the state auditor driven from the monopolistic market share of the state auditor in relation to SOEs. Additionally, many other differences exists between the present study and the research of Azizkhani et al., for instance the present study employs several robustness and additional tests to corroborate the main findings.

In addition, whereas prior studies focus primarily on the effects of the increased concentration in audit markets as a result of the mergers of the Big audit firms and the Arthur Andersen closure, the audit market liberalization has resulted in an interesting research setting to study the effects of increased competition in the Iranian audit market. More importantly, intense competition occurs in an audit market in which auditors cannot gain market power by quality differentiation due to the lack of demand for high quality audit services. Hence, the present study can extend existing literature by studying the effect of increased competition in an unfavorable audit market on audit fees. The findings of the present study suggest that the negative effect of weak demand for high quality audit services on audit fees can be exacerbated by increased competition in the audit market.

Although the Iranian audit market provides a somewhat unique research setting to study the effect of auditor type and competition among auditors on audit fees, the findings of the present study not only support extant literature, but are also generalizable to a certain extent. In particular, the findings of the present study can be generalized to audit contexts characterized by low demand for high quality audit services and intense competition among auditors, especially small size auditors. The audit market share of small size audit firms (not Big auditors) in most audit markets can be perceived to have the aforementioned characteristics. More importantly, while the lack of competition in most audit markets is flagged as a problem by policymakers (e.g., European Commission in October 2010)⁴ and policymakers may attempt to increase the level of competition in audit markets, the present study

³ The combined disclosed audit fees by clients, after audit market liberalization, also contain fee of tax auditing, whereas auditors were not allowed for tax auditing before audit market liberalization.

⁴ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0561:FIN:EN:PDF>



suggests that the negative effect of low demand for high quality audit services can be worsen by increased competition. Very low audit fees may results in a doubt about the quality of audit services provided by auditors.

The remainder of the present paper proceeds as follows. The contemporary audit market of Iran and relevant institutional factors (i.e., demand for audit services and litigation risks) are briefly reviewed in Section 2. The section also develops the research hypotheses. The sampling design and model specification form Section 3. Section 4 presents the findings of the descriptive analysis and multivariate analysis, as well as the results from the robustness and additional tests. The conclusion and final remarks are provided in Section 5.

2. BACKGROUND AND HYPOTHESES DEVELOPMENT

2.1 The Iranian audit market

Both national and international audit firms operated in Iran prior to the Islamic Revolution in 1979. Following the revolution, the nationalization program resulted in a lack of demand for the services of private audit firms. Three semi-state audit firms were established to audit newly nationalized firms: the Nationalized Industries and Plan Organization Audit Firm (1980); the Mostazafan Foundation Audit Firm (1981); and the Shahed Audit Firm (1983). The IAO was established as a state body by merging the three audit firms in 1987 in an effort to deal with the lack of comparability in the audited annual reports by three aforementioned audit firms (Mashayekhi and Mashayekh, 2008; Roudaki, 2008). Privatization policies have been adopted by the Iranian government to promote economic growth since 1988, which marks the end of the war between Iran and Iraq. Hence, the IAO's responsibility for auditing a large number of SOEs, coupled with an increasing number of private firms because of the privatization policies, resulted an insurmountable workload for the auditor (Azizkhani, 2011).

To respond to the new needs of Iran following the end of the war and decrease the insurmountable workload of the IAO, the Iranian Parliament ratified the 'Using Services of Certified Public Accountant Act' (USCPAA) in 1993. Certified public accountants are allowed to provide audit services to the public sector in accordance with the Act. However, the Act was not operationalized until late 2001. As a result, the Iranian audit market continued to be dominated by the IAO from 1993 until 2001. Auditing market liberalization actually began with the founding of the IACPA, in accordance with the Act, in late 2001. Audit market liberalization resulted in the establishment of a large number of private audit firms that would become members of IACPA (Bagherpour et al., 2008). Every year, new audit firms are established and become members of the IACPA, adding to the number of private audit firms operating within the Iranian audit market. By April 2013, 253 private audit firms were listed as members of IACPA.⁵ The rapid increase in the number of private audit firms and the monopolistic audit market share of the IAO in relation to SOEs have resulted in intense competition in the Iranian audit market, particularly among private auditors.⁶ The continued support from the Iranian government for the IAO has resulted in a portion of the Iranian audit market being monopolized by the IAO. In accordance with note 5 of USCPAA, private audit firms, as members of the IACPA, can be selected by SOEs as external auditors. In contrast with the Act, the circular of Ministers Council in early 2002 mandates that the audit work of firms with at least 50 per cent of their shares being owned by the state must be audited by the IAO (Hoshi, 2012).

⁵ www.iacpa.ir

⁶ The argument that no equal growth on the demand and supply sides of the audit market exists appears to be in contrast with economics theories. However, in the absence of any empirical evidence, the greater growth on the supply side of the Iranian audit market can be attributed to the existence of four distinct factors: the relatively easy requirements for establishing private audit firms (Roudaki, 2008); the establishment of audit firms by prior audit managers of the IAO following the decrease in salary and remunerations by the IAO; the existence of rumors concerning a potential new demand for auditing services (mandatory tax auditing for all entities); and some cultural elements, including the lack of willingness for individuals to work as part of a team (Deilampoure, 2012).



The rapid growth on the supply side of the Iranian audit market, especially in relation to private audit firms, has resulted in intense competition among the auditors. Increased competition in the Iranian audit market provides an opportunity for clients to engage in realignment activities because more options are now available for clients. Such an argument is consistent with the findings of Bagherpour et al. (2008), who provide evidence that auditor switching dramatically increased following audit market liberalization. Additionally, some practitioners warn about the wrongful competition regarding audit fees among private auditors due to client shortfall (Bozorg Asl, 2010).

2.2 Institutional background

Since the general lack of adequate knowledge concerning the audit environment of Iran appears evident, a brief discussion concerning the demand for audit services and litigation risks in the Iranian audit market provides useful background information. The discussion regarding the demand for audit services and litigation risks in Iran can explain why client firms place greater emphasis on audit fees in their realignment decisions.

Two types of firms are listed on the TSE: SOEs and non-state firms (non-SOEs). In many instances, the firms are characterized by concentrated ownership. The owners, who also serve as board members or CEOs, have virtually complete access to information concerning the firms. This situation results in negligible information asymmetry (Mohammadrezaei et al., 2012). Hence, due to a lack of intense agency problems, corporate auditing is not perceived as a necessity by the concentrated shareholders. Additionally, other players, such as minority shareholders, creditors and the capital market,⁷ are less likely to play a significant role in motivating Iranian firms to demand high quality audit services. For instance, the evidence provided by Hassas Yeganeh (2006) indicates that minority shareholders behave as speculators and strive for short-run benefits without any propensity or effort to be involved in directing the firm. Meanwhile, the lack of a sufficient legal framework to support shareholders' desires to have supervisory roles in directing the activities of firms is apparent. Briefly, concentrated shareholders consider corporate auditing as a purely legal requirement and the shareholders must bear a large portion of the costs without much benefit (Hovansian Far, 2010a). In such a scenario, the demand for audit services is primarily driven by certain laws that impose rules regarding the appointment of auditors in Iran, such as the Security Market Act (1967); the IAO establishment act (1983); and the USCPAA (1993). This is consistent with the following excerpt:

“the corporate auditor’s role in this respect is legitimated and given authority by the mandatory requirements of state regulators for a professional audit, and satisfies the political role of such regulators as guardians of public interest- they are seen to be putting mechanisms such as audit in place to monitor and control corporate behaviors” (Flint, 1988, p. 41).

The argument above indicates the low demand for high quality audit services in Iran.⁸ When the demand for audit services is mainly driven by legal requirements, client firms will have a significant tendency to comply with the legal requirements while bearing minimum costs (paying low audit fees).

Another important institutional factor in the Iranian audit market is litigation risk. Similar to the demand for audit services, the lack of strict litigation risks is evident in Iran. The legal responsibilities of auditors in Iran are determined by certain laws concerning civic responsibilities and criminal responsibilities. For instance, Article 267 of the Trade Law provides that if an auditor deliberately reports erroneous information about a firm to an annual general meeting, the auditor will face up to two years in prison (Vafadar Zadeh, 2011). It seems that a sufficient legal basis may exist that could be applied to enhance litigation risk. However, in practice, the motivation of Iranian auditors for opportunistic behaviors is less likely to be hindered by litigation risks (Dehkordi and Makarem, 2011). In addition, the cancelation of a CPA license by the IACPA due to audit failures is the most significant risk,

⁷ Consistent with the present discussion, DeFond et al. (2000) argue that few institutional characteristics exist in the Chinese capital market that create or motivate demand among managers for external auditing.

⁸ Consistent with the present discussion, DeFond et al. (2000) highlight the low demand for independent auditors in China.



which seldom occurs (Mahmudi, 2010). It is noteworthy that the lack of strong litigation risks in Iran may be attributable to the lack of proper demand for high quality audit services. It can be argued that the negative effect of the low demand for high quality audit services and weak litigation risk on audit fees may be exacerbated by the rapid increased competition in the Iranian audit market.

2.3 Hypothesis development

2.3.1 Auditor type

Prior studies have investigated the effect of different types of auditors such as Big versus non-Big auditors (e.g., Palmrose, 1986; Caneghem, 2010) and industry specialized versus non-specialized auditors (e.g., Scott and Gist, 2013) on audit fees. The studies employ different views to explain audit fees differences between different types of auditors including auditor's reputation, product differentiation and industry specialization (e.g., Palmrose, 1986; Francis and Wilson, 1988; Scott and Giston, 2013). Since audit market structure is different for private and state auditors in Iran, the present study hypothesizes the effect of auditor type in Iran on audit fees in light of market power view.

Audit market of Iran is intensely competitive for private auditors, but it is also monopolized, in part, by the state auditor at the same time. Economics theory states that pricing strategies are significantly different in competitive markets compared with those in monopolistic markets. In the present study, an audit market is considered to be a market characterized by perfect competition for private auditors when: (i) there are many private audit firms; (ii) demand for audit services exists that is mainly driven by legal requirements; (iii) there is low of demand for high quality audit services, resulting in audit services being perceived as homogenous from the perspective of consumers; and (iv) audit fees of private auditors are not same, but still similar to one another. Hence, in light of the economics theory, private auditors are more likely to have zero market power⁹ in setting audit fees. In other words, private auditors should be price takers. The price is determined by an interaction between demand and supply at the market level. If one private audit firm strives to set audit fees above market level, its clients will leave the audit firm and acquire audit services at the market price from other private auditors. Since the competitive audit market environment of private auditors provides more options for client firms and the clients are less likely to place great emphasis on audit quality, low audit fees are recognized as the best way to retain clients and to attract new ones.

As discussed earlier, a portion of the Iranian audit market is relatively monopolized¹⁰ by the state auditor (IAO). 'Legal barriers' provide a monopolistic audit market for the IAO in relation to SOEs (Esaae-khosh, 2011). While the IAO has significant market power, the power is not unlimited because the state can interfere if the IAO charges significantly abnormal audit fees. Audit fees are set by the state auditor based upon its circumstances and not the interaction between demand and supply. Since a monopolistic supplier is not concerned with potentially losing its market share to competitors, such a supplier can set prices considerably higher than marginal costs. Monopolistic situations provide the opportunity for suppliers to set prices that are usually higher than the prices in a competitive market (e.g., Kahana and Katz, 1990; Langbien and Willson, 1994; Mises, 1998). Hence, the first hypothesis is as follows:

Hypothesis 1 (H₁): Compared with the state auditor, audit fees are lower for private auditors.

2.3.2 Audit market competition

⁹ Market power refers to the ability to increase the product's price above marginal costs without losing all customers.

¹⁰ A monopoly is a structure in which only a single supplier produces and sells a given product in a given market.



Audit market structure (competition or concentration) has attracted the attention of both policy makers and researchers due to the increased concentration in audit markets following the mergers of the Big audit firms and the scandal of Arthur Andersen. Government Accountability Office (GAO) (2003) investigation reveals that limited and mixed evidence exist regarding the effect of audit market concentration on auditor independence, audit fees, audit quality, competition and client choice. Numan and Willekens (2012) argue that no consensus exists concerning the proper structure of an audit market, particularly in regards to competition and concentration.

Consistent with structure-conduct-performance framework¹¹ (Bain, 1951), most prior studies find that audit fees decrease as competition increases in an audit market (e.g., Bandyopadhyay and Kao, 2001; Jensen and Payne, 2005; McMeeking, 2007; Chen et al., 2007; Behn et al., 2009). The findings of Chen et al. (2007), in the context of China, reveal that Big audit firms gain considerable fee premiums in less competitive supplementary markets. However, audit fee premiums are not significant for Big audit firms in the competitive statutory market. Along similar lines, other studies find that increased concentration in an audit market has a positive effect on audit fees (e.g., Menon and Williams, 2001; Ding and Jia, 2012; Carson et al., 2012). Ding and Jia (2012) find that audit fees for Big audit firms increase following increased concentration in the UK audit market due to the PricewaterhouseCoopers merger. The authors suggest that the market power view has more explanatory power than cost savings from the merger in relation to explaining audit fees strategies utilized following increased concentration in the audit market. However, Pearson and Trompeter (1994) and Ivancevich and Zardkoohi (2000) find a negative effect of the mergers of audit firms on audit fees. Generally, both theoretical and empirical evidence indicate that increased competition in an audit market is more likely to result in decreased audit fees.

Following audit market liberalization in late 2001 and over research period not only competition increased among private auditors, but also monopolistic market share of the state auditor decreased (see Panel C of Table 2). In particular, although the market share of private auditors increased over research period, the number of private auditors also increased simultaneously. More specifically, the increase in supply side is greater than demand side in the competitive audit market share of private auditors (see Panel C of Table 2). Hence, the number of client per auditor (market share of each auditor) decreased over research period for private auditors. In light of the findings of prior studies, as referred above, increased competition results in low audit fees. This is the case because clients have more choice and auditors have less market power. In regards to the state auditor, the market share of the auditor decreased from about two-third to about one-third of Iranian audit market (see Panel C of Table 2). That is, the monopoly power of the state auditor decreased over research period. The auditor knows that his market power decreased over time because a part of his clients switches to private auditors with lower fees. As a result of decreased market power, the state auditor may be motivated to set lower audit fees in an effort to retain clients, especially clients who have choice such as semi-state firms. Consistent with the prior studies, it can be concluded that increased competition in the Iranian audit market is more likely to result in lower audit fees.¹² Therefore, the second hypothesis is as follows:

Hypothesis 2 (H₂): Audit fees decrease as competition increases in the Iranian audit market.

3. RESEARCH DESIGN

3.1 Sampling design

¹¹ The market structure affects a firm's behavior in terms of quantities and prices, and, hence, profits. An increase in competition results in a decrease in a firm market share, price and profits (Schmidt, 1997).

¹² Our argument may be criticized because Shaked and Sutton (1982) show that quality differentiation can relax price competition. However, this seems not be case because low demand for high quality audit services exists in the Iranian audit market. Hence, in the competitive audit market of Iran auditor are less likely to obtain market power by quality differentiation.



Data was collected regarding audit fees, auditor types and other characteristics of client firms from the annual reports of firms listed on the TSE between 2001 and 2010. The annual reports are available on the website of the Research, Development and Islamic Studies (RDIS)¹³ of the Securities and Exchange Organization and the CD-ROM database of annual reports, which are also produced by the RDIS. Since audit market liberalization occurred in late 2001, the period of 2001 to 2010 is selected. Moreover, consistent with the arguments of Bagherpour et al. (2008), many annual reports prior to 2001 are “incomplete and had pages removed” (p.11). Furthermore, since the disclosure of audit fees is voluntary during the research period, any firms failing to make voluntary disclosures concerning audit fees are excluded from the sample. The final sample contains 1,208 firm-year observations from the years 2001 to 2010. The study period ends in 2010 for several reasons, one of which concerns the changes in institutional factors in the research context. In particular, although the potential influence of changes in institutional factors during the research period is controlled for by adding year dummies to the research models, the changes in the political and economic environment after 2010 appear to be significant. For instance, significant economic sanctions have been imposed in recent years that are likely to influence the performance of firms. As a result, the Iranian currency (Riyal)/U.S. dollar exchange rate has decreased more than threefold compared to the period prior to the sanctions. This has had considerable effects on the economy at both the macro and micro levels. Such a situation is more likely to influence firm performance and the Iranian audit market itself. However, this is an issue which is beyond the scope of the present study. The sample selection process is presented in Table 1.

TABLE 1 SAMPLE SELECTION.

	Total Sample
Initial observations (from 2001 to 2010)	3,384
Less: firms delisted	151
Less: financial institutions	321
Less: observations with missing value on financial information or other control variables to be adopted in the present study	384
Subtotal: number of observations with available data	2,528
Less: observations with no audit fees data	1,320
Observations in final analysis	1,208

3.2 Model specification

3.2.1. Exogenous auditor choice

To test the hypotheses, two regression models are utilized. Model (1) tests the relationship between auditor type and audit fees (H_1), while Model (2) examines the relationship between audit market competition and audit fees (H_2). The regression models are as follows:

$$\begin{aligned}
 \text{Logfee}_{it} = & \beta_0 + \beta_1 \text{Audpvt}_{it} + \beta_2 \text{Opinion}_{it} + \beta_3 \text{Audchg}_{it} + \beta_4 \text{Size}_{it} + \beta_5 \text{Lev}_{it} + \beta_6 \text{InvRec}_{it} \\
 & + \beta_7 \text{Liq}_{it} + \beta_8 \text{Issue}_{it} + \beta_9 \text{ROA}_{it} + \beta_{10} \text{Loss}_{it} + \beta_{11} \text{Subs}_{it} + \beta_{12} \text{Busy} \\
 & + \beta_{13} \text{Conown}_{it} + \beta_{14} \text{NStown}_{it} + \beta_{15} \text{SStowm} + \sum \beta_j \text{IndustryDum} + \beta_k \text{YearDum} + \varepsilon_{it}
 \end{aligned}
 \tag{1}$$

¹³ <http://www.rdis.ir/CMPAnnouncements.asp>



$$\begin{aligned}
 \text{Logfee}_{it} = & \beta_0 + \beta_1 \text{Herf}_{it} + \beta_2 \text{Opinion}_{it} + \beta_3 \text{Audchg}_{it} + \beta_4 \text{Size}_{it} + \beta_5 \text{Lev}_{it} + \beta_6 \text{InvRec}_{it} \\
 & + \beta_7 \text{Liq}_{it} + \beta_8 \text{Issue}_{it} + \beta_9 \text{ROA}_{it} + \beta_{10} \text{Loss}_{it} + \beta_{11} \text{Subs}_{it} + \beta_{12} \text{Busy} \\
 & + \beta_{13} \text{Conown}_{it} + \beta_{14} \text{NStown}_{it} + \beta_{15} \text{SStowm} + \sum \beta_j \text{IndustryDum} + \beta_k \text{YearDum} \\
 & + \varepsilon_{it}
 \end{aligned} \tag{2}$$

Variables' definition is presented in Appendix. The principal coefficient of interest is β_1 in Model (1) and Model (2), and it is expected that it should be negative and positive for Model (1) and (2), respectively. The effects of a subset of firms' specific factors and auditor-related factors on audit fees are controlled for in Model (1) and Model (2) in light of prior studies (e.g., Simunic, 1984; Hay et al., 2006; Blankley et al., 2012). Some variables are not included in the two models employed in the present study, such as Big 4 audit firms, foreign investor, audit committee, and board independence. While the effects of these variables are controlled for in prior studies, such variables cannot be included as a result of the unique circumstances of auditing and financial reporting in Iran. First, since the Islamic Revolution, international audit firms have not operated in the Iranian audit market. Second, the level of foreign investment is negligible. Third, the disclosure of board independence is not yet compulsory in Iran. Finally, the establishment of audit committees is not yet mandatory, even for listed firms on the TSE.

Consistent with prior studies, the natural logarithm of total audit fees (*Logfee*) is applied to test the hypothesis (e.g., DeFond et al. 2002; Whisenant et al. 2003; Francis and Wang 2005; Ghosh and Pawlewicz 2009; Choi et al. 2010; Stanley, 2011; Blankley et al., 2012). Due to hyperinflationary economy of Iran, we replace *Logfee* with audit fees deflated by total assets to control the effect of inflation in robustness tests section.

As discussed earlier, following audit market liberalization both private audit firms and the state audit firm, IAO, operate in the Iranian audit market. Hence, to investigate the effect of auditor type on audit fees, *Audpvt* is equal to 1 for firms audited by private audit firms and 0 for firms audited by the IAO.

Prior studies measure the concentrated level of audit market at both the country and city level, using a Herfindahl index (e.g., Boone et al., 2012; Francis et al., 2013). Herfindahl index is computed as the sum of the squares of the ratios of each audit firm's size to the total size of the audit market. The size of auditor or audit market can be measured by audit fees, client numbers and so on. It is worth noting that when Herfindahl index is computed yearly, it provides a value as the concentration in audit market level for each year. Hence, if this study applies the original form of Herfindahl index yearly, it will result only in 10 values that will show concentration level in the Iranian audit market in each year (from 2001 to 2010). However, due to the lack of enough variation in relation to concentration level computed by Herfindahl index, it would not provide significant result in regression analysis. To deal with such problem, Francis et al. (2013) compute Herfindahl index in 42 country-industry level. The number of industry groups is low for the present study; and Herfindahl index does not usually vary for an industry group year by year. Such argument indicates that this study is less likely to apply the standard form of Herfindahl index in the case of Iranian audit market. Hence, the present study modifies Herfindahl index to compute concentration in audit firm level instead of audit market level. That is, the modified Herfindahl index is computed as the ratio of each audit firm's size to the total size of the audit market. Such modified Herfindahl index computes market share of each audit firm in each year. The present study computes concentration level in audit firm level (*Herf*) by using: (i) modified Herfindahl index based on number of client firms (*HerfNum*); (ii) modified Herfindahl index based on aggregate size of client firm's assets (*HerfAsset*); and (iii) modified Herfindahl index based upon client firms' revenues (*HerfSale*). In light of the second hypothesis, it is expected that competition (1- concentration) in audit firm level is positively (negatively) associated with audit fees.

Since the pairwise correlation between auditor type (*Audpvt*) and competition in audit firm level (*Herf*) is close to the controversy threshold of 0.80 (see Gujarati, 1995, p. 335), we develop two different models to test the research hypotheses. Such high correlation is expected because audit market share of the state auditor is significantly high compared with private auditors (see Panel C of Table 2). Although there is high correlation between *Audpvt* and *Herf*, the variables obviously measure different things. *Audpvt* as a dummy variable is employed to test the effect of auditor type on audit fees, whereas *Herf* as a continuous variable is included in Model (2) to test the impact of competition in audit firm level on audit fees. In robustness tests section, we re-estimate Model (2) for clients of private auditors, separately.



3.2.2 Endogenous auditor choice

Theoretical studies indicate that clients self-select their auditors (e.g., Datar et al. 1991). Hence, following Chaney et al. (2004), a two-stage procedure is utilized in an effort to correct for self-selection bias. In the first stage, a probit regression of the binary dependent variable *Audpvt* on variables that affect auditor choice is run to obtain consistent estimations. Then, the estimations are used to calculate the Inverse Mills Ratios (IMR). Later, in the second stage, Model (1) is re-estimated by including IMR as an additional explanatory variable. The following first-stage self-selection model is developed based upon prior studies (e.g., Chaney et al., 2004; Liu and Subramaniam, 2012):

$$Audpvt_{it} = \lambda + \gamma_1 NStown_{it} + \gamma_2 SStown_{it} + \gamma_3 Size_{it} + \gamma_4 Lev_{it} + \gamma_5 InvRec_{it} + \gamma_6 Liq_{it} + \gamma_7 Loss_{it} + \gamma_8 Curr_{it} + \gamma_9 Salegrowth_{it} + \gamma_{10} Aturn_{it} + \sum \beta_j IndustryDum + \beta_k YearDum + \delta_{it} \quad (3)$$

Variables' definition is presented in Appendix. It is noteworthy that ownership structure can be coded in three categories: non-state ownership (*NStown*); state ownership (*Stown*); and semi-state ownership (*SStown*). Ownership structures are categorized in such a fashion mainly due to the different levels of choice available to the three aforementioned firms. In particular, SOEs may only choose the state auditor. However, although non-SOEs principally choose private auditors (Bagherpour et al., 2008), such clients can also choose the state auditor. A part of semi-state firms appear to be free from the influence of their ownership (state subsidiaries) and choose the private auditors, while other semi-state firms appear to be under pressure to choose the state auditor.

The propensity-score matching models developed by Rosenbaum and Rubin (1983) are also applied as an alternative method to control for self-selection bias. This is due to the fact that IMR is criticized in prior studies (e.g., Lennox et al., 2012) because of its weaknesses in controlling for self-selection bias. Consistent with prior studies in the accounting field (e.g., Lawrence et al., 2011; Campa, 2013), Model (3) is employed to estimate the probability of selecting private auditor (*Audpvt*). Then, we match – without replacement – a client of a private auditor with a client of the IAO (the state auditor) using the nearest neighbor matching procedure. Finally, Model (1) is estimated based upon the propensity-score matched sample.

3.3 Control variables

Audit fees are modeled in prior studies as a function of size; complexity; risk; the type of auditor; additional work; and monitoring. The audit fees models in the present study are developed in light of prior studies (e.g., Simunic, 1984; Larcker and Richardson, 2004; Hay et al., 2006; Gonthier-Besacrier and Schatt, 2007; Al-Harshani, 2008; Liu and Subramaniam, 2012; Doa et al., 2012; Blankley et al., 2012; Carson et al. 2012; Ding and Jia, 2012) and by taking to account the research setting circumstances.

More complex clients should pay higher audit fees. Client complexity is controlled for by including client size (*Size*) and client's subsidiaries (*Subs*) in the audit fees models employed in the present study. Prior studies (e.g., Whisenant et al., 2003) suggest that audit fees should be lower during the initial engagement. Hence, auditor change (*Audchg*) is included in the research models. The possible influence of client risk on audit fees is controlled for by liquidity (*Liq*), return on assets (*ROA*), loss (*Loss*) and leverage (*Lev*). Auditors are more likely to charge higher audit fees for riskier clients. Auditors must spend more time examining receivable confirmation; inventories; equity issues; and the issuance of modified audit opinions. Hence, auditors charge higher audit fees in such circumstances. The effect of client receivables and inventories (*InvRec*), the issuance of new equity (*Issue*) and modified audit opinions (*Opinion*) is controlled for. Consistent with Blankley et al. (2012), the possible influence of the busy season (*Busy*) on audit fees is controlled for. Audit fees are expected to be higher for clients with a fiscal year-end during the busy season. Niemi (2005) concludes that less information asymmetry, less audit risk and



organization complexity are the characteristics of manager-owned firms (*NStown*) and result in low audit fees. SOEs (*Stown*) may have less bargaining power because the firms do not have choice and must choose the state auditor. Semi-state firms (*SStown*) may pay audit fees less than SOEs, but more than non-SOEs because agency problems seem to be higher in semi-state firms compared with non-SOEs.

4. RESULTS

4.1 Descriptive statistics

The descriptive statistics of the research variables are shown in panels A, B and C of Table 2. Panel A presents the descriptive statistics of the continuous variables. In an effort to mitigate the effect of outliers, all continuous variables are winsorized at the 1% and 99% levels. Panel A of Table 2 shows that the mean of leverage (*Lev*) is 72%. The finding is consistent with the findings of Moayed and Aminfard (2012) and the arguments of Mohammadrezaei et al. (2013), who note that the financing system in Iran is close to the “credit-insider” system.¹⁴ Mean ownership concentration (where the firm’s owner holds the largest portion of a firm’s shares) is 56%, which demonstrates a high level of ownership concentration because the corporate governance characteristics of Iran are similar to “insider governance” systems.¹⁵

The univariate analysis of difference in the audit fees between private and state auditors is shown in Panel B of Table 2. The table indicates that the mean *Logfee* is lower for firms audited by private audit firms (*Audpvt*), which is consistent with the first hypothesis of the present study (H_1). Panel B of Table 2 reveals that the mean of market share of the state auditor is significantly higher than the mean of market share of private auditors. Additionally, the clients of private auditors are significantly smaller in size; are less liquid; have less profitability; exhibit lower ownership concentration; and are less likely to have fiscal year ends during the busy season. Panel B of Table 2 also represents that the clients of private auditors are more likely to receive qualified audit opinions;¹⁶ engage more frequently in auditor switching; have more loss; more subsidiaries; less fiscal-year end in busy season; and be non-state owned and semi-state firms.

TABLE 2. DESCRIPTIVE STATISTICS

<i>Panel A: Continuous Variables</i>					
	Mean	Median	SD	Maximum	Minimum
Variables					
<i>Logfee</i>	5.24	5.20	0.72	7.60	3.47
<i>Audit fees</i> (\$)	30,875	22,750	27,000	249,750	4,250
<i>HerfNum</i>	0.15	0.04	0.20	0.65	0.00
<i>HerfAsset</i>	0.20	0.03	0.27	0.77	0.00
<i>HerfSale</i>	0.21	0.03	0.28	0.77	0.00
<i>Size</i>	12.23	12.19	1.17	16.14	9.82
<i>Total assets</i> (000\$)	54,874,500	24,712,625	111,733,375	1,370,591,750	2,364,625
<i>Lev</i>	0.72	0.71	0.24	1.76	0.24
<i>InvRec</i>	0.53	0.56	0.20	0.93	0.07
<i>Liq</i>	1.19	1.09	0.76	4.04	0.07
<i>ROA</i>	0.11	0.10	0.14	0.52	-0.28

¹⁴ In the “credit-insider” system, financing is obtained primarily from the banks and the state. However, in an “equity-outsider” system, financing is principally obtained from the public and capital markets (see, Nobes, 1998).

¹⁵ Because of weak investor protection laws, concentrated ownership is prevalent in Iran. Surveys conducted by TSE managers and the Parliament Research and Development Center during the first decade of the twenty-first century reveal that foundation groups and the Iranian government are the controlling shareholders of most of the firms listed on the TSE (see Mashayekhi and Mashayekh, 2008).

¹⁶ Although the ratio of modified audit opinions for sample firms seems to be surprising, it is comparable with the descriptive findings of other studies in the context of Iran. The descriptive statistics of Anvarkhatibi et al. (2012), Banimahd and Beigi (2012) and Banimahd et al. (2013) find that 64%, 70% and 58% of the audits on firms listed on the TSE consisted of modified audit opinions, respectively.



<i>Conown</i>	0.56	0.54	0.24	1.00	0.00	
<i>Panel B: Univariate test of differences</i>						
Continuous variables-(t-Test)			Dichotomous variables-(Chi-Square test)			
	Private auditors (n=796)	The state auditor (n=412)	<i>t</i>	Private auditors (n=796)	The state auditor (n=412)	Chi-Square
Variables				Variables		
<i>Logfee</i>	5.13	5.44	-6.71***	<i>Opinion</i>	622	251
<i>HerfNum</i>	0.03	0.39	-41.14***	(%)	(78)	(61)
<i>HerfAsset</i>	0.03	0.54	-54.83***	<i>Audchg</i>	138	6
<i>HerfSale</i>	0.03	0.50	-62.00***	(%)	(17)	(1)
<i>Size</i>	12.19	12.31	-1.71*	<i>Issue</i>	215	99
<i>Lev</i>	0.73	0.71	1.24	(%)	(27)	(24)
<i>InvRec</i>	0.53	0.53	-0.21	<i>Loss</i>	124	38
<i>Liq</i>	1.14	1.28	-2.58***	(%)	(16)	(9)
<i>ROA</i>	0.10	0.13	-3.38***	<i>Subs</i>	136	37
<i>Conown</i>	0.52	0.65	-10.01***	(%)	(17)	(9)
				<i>Busy</i>	536	336
				(%)	(67)	(82)
				<i>NStown</i>	307	16
				(%)	(39)	(4)
				<i>SStown</i>	418	134
				(%)	(53)	(33)

Panel C: Audit market share

Year	Full sample	The state auditor			Private auditors					
	Number of sample firms	Number of clients	<i>HerfNum</i> (%)	<i>HerfAsset</i> (%)	<i>HerfSale</i> (%)	Number of private audit firms	Number of clients	<i>HerfNum</i> (%)	<i>HerfAsset</i> (%)	<i>HerfSale</i> (%)
2001	134	86	65.22	76.51	76.85	48	34.78	23.49	23.15	
2002	137	68	50.79	72.20	71.52	42	69	49.21	27.80	28.48
2003	135	50	36.80	59.17	60.60	55	85	63.20	40.83	39.40
2004	134	42	29.60	44.01	49.58	69	92	70.40	55.99	50.42
2005	128	38	28.23	44.18	48.31	70	90	71.67	55.82	51.69
2006	126	31	23.53	39.61	43.30	72	95	76.47	60.39	56.70
2007	112	29	22.25	34.87	40.38	73	83	77.75	65.13	59.62
2008	111	26	22.44	36.34	40.33	77	85	77.56	63.66	59.67
2009	105	23	22.26	31.31	34.49	86	82	77.74	68.69	65.51
2010	86	19	19.27	29.52	30.69	92	67	80.73	70.48	69.31

Note: *, ** and *** denote significance at the 0.10, 0.05 and 0.01 levels, respectively.

Panel C of Table 2 shows the market share of private and state auditors, which is almost consistent with the prior discussion concerning audit market structure in the Iranian audit market. The state auditor's market share, based upon the number of clients (*HerfNum*), decreased over the research period from 65.22% in 2001 to 19.27% in 2010.¹⁷ Although the state auditor's market share is 19.27% in 2010, it is at the same time 29.25% and 30.69% on the basis of clients' total assets (*HerfAsset*) and clients' revenue (*HerfSale*). This indicates that, although the state auditor's market share decreased dramatically following audit market liberalization, the state auditor has continued to audit SOEs, which are significantly larger in size than the clients of private auditors (Iran Manesh, 2006).

Though the market share of private auditors increased over research period,¹⁸ the continuous increase in the number of private auditors must also be considered. Private audit firms can be categorized into two groups: (i) trustee private auditors of the Securities and Exchange Organization; and (ii) non-trustee private auditors. Only

¹⁷ *HerfNum*, *HerfAsset* and *HerfSale* are measured based upon the audit market of firms listed on TSE, not based upon data regarding sample firms. This is the case because sample firms are about one-third of all firm listed on TSE. Hence, analyzing of market share based upon only sample firms is more likely to result in misleading findings.

¹⁸ This is the case because the listed firms on the TSE have a tendency to change their auditors from the state auditor to private audit firms for a variety of reasons, including paying lower audit fees, which is consistent with the findings of Bagherpour et al. (2008). Additionally, due to the market liberalization of the SOEs over research period (see, Mashayekhi and Mashayekh, 2008), the share of the Iranian audit market monopolized by the IAO has decreased.



trustee private audit firms are allowed to provide audit services to firms listed on the TSE. Almost half of private audit firms as members of IACPA are accepted by the Securities and Exchange Organization as trustee auditors, based upon the quality criteria established by the Securities and Exchange Organization.¹⁹ The number of private audit firms depicted in Panel C of Table 2 consists only of private auditors accepted by the Securities and Exchange Organization as trustee audit firms. This indicates that, although private auditors' market share increased over the research period, the number of such firms also increased. For instance, the market share of private audit firms (*HerfNum*), based upon the whole of audit market of listed firms on TSE, increased approximately 13.60%, but the number of private audit firms increased by approximately 25% during the same period. This indicates that the growth in private audit firms is higher than the growth in the market share of trustee audit firms. Such finding indicates that competition increased among private audit firm continuously following audit market liberalization for private audit firms.

In untabulated tests, none of the pairwise correlations of the research variables do not surpass the controversy threshold of 0.80 (see Gujarati, 1995, p. 335), and all variance inflation factors are within normal levels. In other words, multicollinearity problems are not intense.

4.2 Multivariate analysis

Table 3 shows the results of the multivariate analyses of the effective factors on audit fees. Consistent with the first hypothesis (H_1), *Audpvt* is negatively associated with *Logfee*. This finding indicates that audit fees are lower for private auditors than the state auditor. That is, private auditors, in the portion of the Iranian market characterized by competition among private auditors, set audit fees significantly lower than the state auditor who possess monopolistic market share regarding the auditing of SOEs. Such findings are consistent with Kahana and Katz (1990) and Langbien and Willson (1994).

TABLE 3. MULTIVARIATE ANALYSIS OF THE RELATIONSHIP BETWEEN AUDITOR TYPE AND AUDIT FEES

Variables	Expected Sign	Model (1)		Model (1) – Heckman (1979) procedure		Model (1) – Propensity-score matched sample	
		Coefficient	T-Stat	Coefficient	T-Stat	Coefficient	T-Stat
<i>Intercept</i>		1.62***	8.10	1.46***	7.45	1.85***	6.94
<i>Audpvt</i>	-	-0.40***	-10.96	-0.43***	-12.06	-0.42***	-10.89
<i>Opinion</i>	+	-0.01	-0.40	-0.02	-0.58	-0.00	-0.07
<i>Audchg</i>	-	0.04	0.97	0.05	1.34	0.04	0.77
<i>Size</i>	+	0.23***	15.84	0.23***	16.33	0.23***	12.97
<i>Lev</i>	+	0.16**	2.39	0.18**	2.56	0.25***	2.87
<i>InvRec</i>	+	0.18**	2.51	0.20***	2.76	0.13	1.51
<i>Liq</i>	-	0.03*	1.68	0.02	1.01	0.02	1.25
<i>Issue</i>	+	-0.04	-1.25	-0.03	-1.18	-0.05	-1.35
<i>ROA</i>	-	0.13	1.08	0.18	1.58	0.27*	1.76
<i>Loss</i>	+	-0.03	-0.66	-0.03	-0.56	0.06	1.04
<i>Subs</i>	+	-0.00	-0.08	-0.01	-0.16	0.04	0.76
<i>Busy</i>	+	0.03	0.94	0.03	0.76	0.01	0.28
<i>Conown</i>	-	-0.04	-0.66	0.03	0.58	-0.05	-0.63
<i>NStown</i>	-	-0.15***	-3.62			-0.06	-0.80
<i>SStown</i>	?	-0.05	-1.37			-0.03	-0.90
<i>IMR</i>				0.04	1.10		
<i>IndustryDum</i>		Yes		Yes		Yes	
<i>YearDum</i>		Yes		Yes		Yes	
<i>VIF Audpvt</i>		2.11		2.00		1.74	
<i>VIF IMR</i>				3.26			
<i>R²</i>		0.72		0.72		0.74	

¹⁹ For instance, the number of IACPA members was 139 audit firms in 2006 (Roudaki, 2008), but only 72 audit firms were trustee auditors. The number of IACPA members was 237 in 2012, but only 110 audit firms were SEO trustee audit firms. Data were not available regarding the number of SEO trustee audit firms prior to audit market liberalization in late 2001.



<i>F-stat</i>	82.28***	82.40***	63.11***
<i>N</i>	1,208	1,208	759

In regards to control variables, Table 3 reveals that audit fees are higher for large clients, which is consistent with the prediction of this study and findings of Doa et al. (2012) and Blankley et al. (2012). Consistent with the prediction of the present study, auditors charge higher audit fees for firms with higher leverage (*Lev*) and higher inventories and account receivables (*InvRec*). Table 3 shows that *NStown* is negatively associated with *Logfee*. This finding indicates that manager-owners of non-SOEs pay lower audit fees in the lack of intense agency problems, which is consistent with the prediction of the present study and findings of Niemi (2005).

By including IMR in Model (1), second stage audit fees regression is developed. Due to collinearity problems, *NStown* and *SStown* are excluded from the second stage regression of Model (1). Such an approach is suggested by Lennox et al. (2012), who argue that “some of the independent variables from the first stage model should be excluded from the second stage model” (Lennox et al., 2012, p. 609). The IMR coefficient is insignificant for the second stage regression of Model (1). The results based upon this regression are consistent with the main findings in Table 3. Furthermore, the results from the propensity-score matched sample for Model (1) are consistent with the main findings.

Table 4 shows that the concentration in audit firm level (*HerfNum*, *HerfAsset* and *HerfSale*) is positively associated with audit fees (*Logfee*), which is consistent with the second hypothesis (H_2). The finding indicates that audit fees increases (decreases) as concentration (competition) increases. Our results are consistent with the findings of prior studies regarding the effect of market structure on audit fees (e.g., Bandyopadhyay and Kao, 2001; Jensen and Payne, 2005; McMeeking, 2007; Chen et al., 2007; Behn et al., 2009; Carson et al., 2012).

TABLE 4. MULTIVARIATE ANALYSIS OF THE RELATIONSHIP BETWEEN AUDIT MARKET COMPETITION AND AUDIT FEES, MODEL (2)

Variables	Expected Sign	Coefficient	T-Stat	Coefficient	T-Stat	Coefficient	T-Stat
<i>Intercept</i>		1.06***	4.40	1.23***	5.84	1.21***	5.83
<i>HerfNum</i>	+	0.40***	6.18				
<i>HerfAsset</i>	+			0.57***	8.73		
<i>HerfSale</i>	+					0.59***	9.38
<i>Opinion</i>	+	-0.05	-1.54	-0.04	-1.22	-0.03	-1.12
<i>Audchg</i>	-	-0.03	-0.82	0.01	0.26	0.02	0.44
<i>Size</i>	+	0.24***	16.48	0.24***	16.18	0.24***	16.09
<i>Lev</i>	+	0.18**	2.40	0.14**	2.00	0.14**	1.98
<i>InvRec</i>	+	0.12*	1.62	0.15**	2.03	0.15**	2.07
<i>Liq</i>	-	0.05***	2.70	0.04**	2.10	0.03**	1.98
<i>Issue</i>	+	-0.05	-1.59	-0.04	-1.41	-0.04	-1.40
<i>ROA</i>	-	0.05	0.39	0.07	0.58	0.07	0.60
<i>Loss</i>	+	-0.04	-0.80	-0.03	-0.70	-0.03	-0.71
<i>Subs</i>	+	-0.04	-0.92	-0.02	-0.51	-0.02	-0.43
<i>Busy</i>	+	0.05	1.52	0.05	1.43	0.05	1.38
<i>Conown</i>	-	-0.05	-0.84	-0.05	-0.83	-0.05	-0.83
<i>NStown</i>	-	-0.30***	-7.24	-0.21***	-5.00	-0.20***	-4.59
<i>SStown</i>	?	-0.15***	-4.50	-0.09***	-2.68	-0.08**	-2.29
<i>IndustryDum</i>		Yes		Yes		Yes	
<i>YearDum</i>		Yes		Yes		Yes	
R^2		0.70		0.71		0.71	
<i>F-stat</i>		72.96***		75.95***		76.77***	
<i>N</i>		1,208		1,208		1,208	

In regards to control variables, liquidity (*Liq*) is positively associated with audit fees, which is in contrast with the prediction of the present study. Such finding may be attributable to that SOEs have higher liquidity compared with non-SOEs and at the same time SOEs pay higher audit fees to the state auditor. In addition, semi-state firms (*SStown*) are negatively associated with audit fees. Other findings regarding control variables are consistent with those represented in Table 3.



4.3 Endogenous auditor choice

Table 5 presents the results of the auditor choice regression, Model (3). Consistent with the discussion in prior sections and empirical evidence provided by Bagherpour et al. (2008), the findings reveal that *NStown* has a positive relationship with *Audpvt*. Additionally, the table shows that semi-state firms (*SStown*) mainly choose private auditors.

TABLE 5. COEFFICIENT ESTIMATE FOR THE AUDITOR CHOICE REGRESSION MODEL

Variables	Coefficient	Z-Stat
Intercept	3.75**	2.15
<i>NStown</i>	5.08***	12.38
<i>SStown</i>	2.73***	12.40
<i>Size</i>	0.32***	-3.01
<i>Lev</i>	-0.73	-1.25
<i>InvRec</i>	-0.17	-0.18
<i>Liq</i>	-1.05***	-5.46
<i>Loss</i>	0.01	0.04
<i>Curr</i>	2.65***	2.62
<i>Salegrowth</i>	-0.17	-0.70
<i>Atum</i>	0.24	1.01
<i>IndustryDum</i>	Yes	
<i>YearDum</i>	Yes	
Pseudo R^2	0.45	
Wald Chi2	312.85***	
<i>N</i>	1,208	

Note: **, *** and **** denote significance at the 0.10, 0.05 and 0.01 levels, respectively.

The IMR is calculated utilizing the estimates from the auditor choice model. As discussed earlier, the IMR is included in the second stage audit fees regression. The White's heteroscedasticity-corrected T and Z statistics are also reported in Tables 3, 4 and 5.

4.4 Robustness tests

4.4.1 Alternative measure of audit fees

With regards to the hyperinflationary economy of Iran and the fact that the clients of the state auditors (SOEs) are significantly larger than the clients of private auditors, we replace *Logfee* with audit fees deflated by total asset (*Feeasset*). The mean *Feeasset* is 0.0000159 and 0.0000123 for the state auditor and private auditors, respectively. The untabulated results based upon *Feeasset* are consistent with the main findings in Table 3 and Table 4. In particular, the results show that the coefficient of *Audpvt* is -0.0008 (t -value=-7.03, p -value<0.001). Additionally, the results reveal that the coefficient of *HerfNum* is 0.0007 (t -value=4.66, p -value<0.001); the coefficient of *HerfAsset* is 0.0012 (t -value=6.41, p -value<0.001); and the coefficient of *HerfSal* is 0.0012 (t -value=6.74, p -value<0.001), following the replacement of *Logfee* with *Feeasset*.

4.4.2 Alternative estimation approaches

The robustness of the findings is tested utilizing alternative estimation approaches. Although the impact of effective factors on audit fees is controlled for in light of extant literature and the circumstances in the Iranian audit market, the present findings are likely be viewed as confounded because of uncontrolled firm-specific variables associated with audit fees. As a result, failure to capture all firm characteristics that determine audit fees may



appear to result in omitted correlated variable bias. To deal with this concern and to corroborate the main findings, certain alternative estimation approaches are performed.

First, Model (1) and Model (2) are re-estimated with standard errors clustered by firm. The results of the re-estimation of Model (1) show that the coefficient of *Audpvt* is -0.40 (t -value=-7.02, p -value<0.001), which is consistent with the main findings. The results of the re-estimation of Model (2) reveal that the coefficient of *HerfNum* is 0.40 (t -value=5.01, p -value<0.001); *HerfAsset* is 0.57 (t -value=6.10, p -value<0.001); and *HerfSale* is 0.59 (t -value=6.48, p -value<0.001), which are consistent with the main findings. The results suggest that the relationship between *Logfee* and *Audpvt*; between *Logfee* and *HerfNum*; between *Logfee* and *HerfAsset*; and between *Logfee* and *HerfSale* is robust to utilizing OLS regressions with clustered standard errors.

Second, Model (1) and Model (2) are re-estimated using firm-fixed effects to capture “omitted time-invariant firm-specific factors” (Ball et al., 2012, p. 156). Such analysis is expected to lower the estimation power of the tests. Nevertheless, the analysis is performed to test whether the relation between; *Logfee* and *Audpvt*; *Logfee* and *HerfNum*; *Logfee* and *HerfAsset*; and *Logfee* and *HerfSale* is could be attributable to time-invariant factors. Table 6 shows that the coefficient of *HerfNum*, *HerfAsset* and *HerfSale* (*Audpvt*) continues to be positive (negative) and significant, revealing that the effect of *Audpvt*, *HerfNum*, *HerfAsset* and *HerfSale* on *Logfee* is robust to including firm-fixed effects. As firm-fixed effects “over-control for the time-invariant determinants” (Ball et al., 2012, p. 161), the coefficients of *Audpvt*, *HerfNum*, *HerfAsset* and *HerfSale* decline in these regressions compared to those reported in Table 3 and Table 4.

Table 6. Multivariate analysis of the relationship between auditor type, audit market competition and audit fees with firm fixed effects

Variables	Model (1)			Model (2)					
	Expected Sign	Coefficient	T-Stat	Coefficient	T-Stat	Coefficient	T-Stat	Coefficient	T-Stat
<i>Intercept</i>		4.97***	7.32	4.68***	8.78	4.70***	6.81	4.72***	6.85
<i>Audpvt</i>	-	-0.23***	-3.94						
<i>HerfNum</i>	+			0.12*	1.70				
<i>HerfAsset</i>	+					0.21**	2.43		
<i>HerfSale</i>	+							0.25***	2.92
<i>Opinion</i>	+	-0.04	-1.27	-0.04	-1.01	0.04	-1.13	-0.04	-1.17
<i>Audchg</i>	-	-0.01	0.47	-0.02	-0.59	-0.00	-0.15	0.00	0.00
<i>Size</i>	+	0.09**	2.04	0.10**	2.23	0.10**	2.16	0.10**	2.12
<i>Lev</i>	+	-0.02	-0.18	-0.00	-0.02	-0.01	-0.06	-0.01	-0.08
<i>InvRec</i>	+	0.20	1.24	0.20	1.23	0.21	1.28	0.21	1.27
<i>Liq</i>	-	0.00	0.17	0.01	0.45	0.00	0.32	0.00	0.25
<i>Issue</i>	+	-0.03	-1.27	-0.03	-1.60	-0.03	-1.47	-0.03	-1.44
<i>ROA</i>	-	-0.03	-0.28	0.05	-0.38	-0.05	-0.37	-0.05	-0.38
<i>Loss</i>	+	-0.03	0.62	0.03	0.65	0.03	0.61	0.03	0.59
<i>Subs</i>	+	-0.05	-0.97	-0.05	-1.05	-0.05	-1.06	0.05	-1.04
<i>Busy</i>	+	0.06	0.74	0.07	0.88	0.07	0.85	0.07	0.82
<i>Conown</i>	-	-0.16	-0.95	-0.23	-1.33	-0.22	-1.28	-0.21	-1.25
<i>NStown</i>	-	-0.18**	-2.21	-0.22***	-2.66	-0.21**	-2.49	-0.20**	-2.41
<i>SStown</i>	?	-0.09*	-1.76	-0.11**	-2.13	-0.11**	-2.06	-0.10*	-1.96
<i>YearDum</i>		Yes		Yes		Yes		Yes	
<i>R²</i>		0.61		0.57		0.58		0.59	
<i>F-stat</i>		44.11***		40.94***		41.06***		41.77***	
<i>N</i>		1,208		1,208		1,208		1,208	

Note: ‘*’, ‘**’ and ‘***’ denote significance at the 0.10, 0.05 and 0.01 levels, respectively.

4.4.3 Differentiation of client assets size

Prior studies suggest that competition among auditors is higher in the small-client market (Francis and Simon, 1987; Chaney et al., 2004). In other words, large audit firms are less likely to obtain significant fee premiums in the small-client market. In order to determine whether the fee premium of the state auditor in the monopolized portion of the Iranian audit market can be attributed to the size of the clients, the sample is partitioned into two subsamples: *small* (firms with total assets less than the median) and *large* (firms with total assets more than the median). With regards to the hyperinflationary economy of Iran, we partition the sample into *small* and *large* in each year. The



median of client size is 12.19 for the full sample. The results of the re-estimations of Model (1) by the *small* sub-sample show that the coefficient of *Audpvt* is -0.43 (t -value=-8.87, p -value<0.001). The results of re-estimations of Model (1) by the *large* sub-sample show the coefficient of *Audpvt* is -0.36 (t -value=-5.87, p -value<0.001). Such findings not only support the main findings, but they also support the notion that the low audit fees of private auditors in the competitive portion of the Iranian audit market is less likely to be determined by client size than by market structure.

4.4.4 Sub-sample analysis

As discussed in ‘models specification section’, we develop two regression models to test the two hypotheses due to the high correlation between auditor type and competition in audit firm level. Our findings regarding second hypothesis may be criticized in the way that there is relationship between competition in audit firm level and audit fees because of the exclusion of auditor type from second hypothesis. To deal with such criticism, we re-estimate Model (2) only within clients of private auditors (796 firm-year observations). By such manner concern regarding the uncontrolled role of auditor type in testing the relationship between competition in audit firm level and audit fees can no longer stand. The results, based upon analysis within clients of private auditors, are consistent with the main findings depicted in Table 4. In particular, the results reveal that the coefficient of *HerfNum* is 0.22 (t -value=1.74, p -value<0.10); the coefficient of *HerfAsset* is 0.29 (t -value=2.24, p -value<0.05); and the coefficient of *HerfSal* is 0.32 (t -value=2.56, p -value<0.05), based upon re-estimation of Model (2) only within clients of private auditors.

Since the state auditor principally performs audit services for SOEs and semi-state firms, a concern exists regarding whether the high audit fees of the state auditor can be attributed to the type of ownership instead of the type of auditor. We, in an effort to account for this concern, re-estimate Model (1) only within semi-state firms (552 firm-year observations) because such firms are audited by both private auditors (418 firm-year observations) and the state auditor (134 firm-year observations). The results, based upon analysis within semi-state firms, are consistent with the main findings depicted in Table 3. In particular, the results reveal that the coefficient of *Audpvt* is -0.37 (t -value=-7.01, p -value<0.001), based upon re-estimation of Model (1) only within clients of semi-state firms.

Since audit fees disclosure is voluntary in Iran, our findings are likely to suffer from selection bias. Obviously, audit fees are available only for firms with voluntary disclosure. In addition, since audit fees are dependent variable, propensity score-matched method and Heckman’s (1979) two stage procedure could not be applied. Hence, t -test and chi-square test are employed to compare the characteristics of firms with voluntary disclosure of audit fees (1,208 firm year observations) and non-disclosed firms (1,320 firm-year observations) to mitigate concern raisin from the voluntary disclosure. A model regarding effective factors on voluntary disclosure of audit fees is developed in light of prior studies (e.g., Lennox, 1999; Bedard et al., 2010).²⁰ The results show that almost there are no significant differences between the characteristics of firms with voluntary disclosure of audit fee compared with those of non-disclosed firms. More specifically, only two differences are detected regarding the characteristics of the two type firms. The size of firms with voluntary disclosure is smaller than that of firms without the voluntary disclosure. In addition, the clients of the state auditor are more likely to disclose audit fees as voluntary.

4.5 Additional tests

²⁰ The model of effective factors on voluntary disclosure of audit fees is developed as follows:

$$\begin{aligned} Disclose_{it} = & \alpha_0 + \alpha_1 Audpvt_{it} + \alpha_2 Audchg_{it} + \alpha_3 Size_{it} + \alpha_4 Lev_{it} + \alpha_5 Loss_{it} + \alpha_6 ROA_{it} + \alpha_7 LogAge_{it} \\ & + \alpha_8 Subs_{it} + \alpha_9 NStown_{it} + \alpha_{10} SStown_{it} + \alpha_{11} Insown_{it} + \alpha_{12} \Delta Management_{it} + \sum \beta_j IndustryDum \\ & + \beta_k YearDum + \varepsilon_{it} \end{aligned}$$



Our findings may be subject a bias raisin from audit quality differences between private and state auditors in testing the effect of auditor type on audit fees. Put differently, the entire of audit fees differences is mistakenly to be attributed to different audit market structures of private and state auditors when there is significant difference between the quality of audit provided by private and state auditors. To deal with this potential problem, we investigate the audit quality of private and state auditors. The modified discretionary accruals model of Dechow, Sloan and Sweeney (1995) by Kothari, Leone and Wasley (2005), discretionary accruals model developed by Ball and Shivakumar (2006) and accrual quality model developed by Dechow and Dichev (2002) are utilized as three measures of audit quality. To obtain industry-specific parameters to compute the non-discretionary components of total accruals, the three models are applied for firms in the same industry (based upon Securities and Exchange Organization's industry classification) in each year. Audit quality model is developed based upon prior studies (e.g., Kallapur et al., 2010; Boone et al., 2012) as follows:

$$\begin{aligned}
 AudQual_{it} = & \beta_0 + \beta_1 Audpvt_{it} + \beta_2 Audchg_{it} + \beta_3 Size_{it} + \beta_4 Lev_{it} + \beta_5 Salegrowth_{it} + \beta_6 Issue_{it} \\
 & + \beta_7 ROA_{it} + \beta_8 Loss_{it} + \beta_9 OCF_{it} + \beta_{10} Subs_{it} + \beta_{11} LogAge_{it} + \beta_{12} Conown_{it} \\
 & + \beta_{13} NStown_{it} + \beta_{14} SStown_{it} + \sum \beta_j IndustryDum + \beta_k YearDum + \varepsilon_{it} \quad (4)
 \end{aligned}$$

Variables' definition is presented in Appendix. Where *AudQual* is absolute discretionary accruals measured by Kothari et al. (2005) and Ball and Shivakumar (2006) model and absolute value of accrual quality measured by Dechow and Dichev (2002) model.

The results show that the audit quality of private auditors is higher than that of the state auditor. In particular, the coefficients for *Audpvt* are; -0.020 (*t*-value=-3.19, *p*-value<0.001); -0.004 (*t*-value=-1.02, *p*-value=0.307); and -0.011 (*t*-value=-2.31, *p*-value<0.05) when audit quality is measured by Kothari et al. (2005), Ball and Shivakumar (2006) and Dechow and Dichev (2002) models, respectively. The results after controlling for auditor choice are similar to the aforementioned results. In conclusion, our main results are less likely to suffer from the potential bias resulted from auditor quality differences because audit quality of the private auditors is higher than the state auditor. As a result, the entire of audit fees difference between state and private auditors are likely to be attributed to different audit market structure (market power) of the auditors.

The aforementioned concern may be generalizable to when we test the effect of competition in audit firm level and audit fees. That is, there is an unsupported premise that quality differentiated auditors can gradually obtain more market share and charge higher audit fees. If it is the case, the entire of audit fees differences is mistakenly to be attributed to different level of competition in audit firm level. To deal with such potential concern, we test the effect of competition in audit firm level on audit quality measured by three aforementioned earnings management proxies. In other words, we replace *Audpvt* with *HerfNum*, *HerfAsset* and *HerfSale* in Model (4). The results show that *HerfNum*, *HerfAsset* and *HerfSale* are insignificantly associated with audit quality. Such findings indicate that audit firms with higher market share are not typically high quality auditors. Hence, such findings do not go against our second hypothesis that audit fees decreases (increases) as competition increases (decreases) in audit firm level.

5. CONCLUSION AND REMARKS

Although prior studies examine the effect of variety of auditor type (e.g., Big vs. non-Big audit firms) and audit market structure (competition and concentration), the lack of empirical evidence regarding the impact of the unique characteristics of the Iranian audit market on audit fees is obvious. The present study examines the impact of auditor type (private vs. state) and audit market competition on audit fees in the emerging Iranian audit market. Using data from firms listed on the TSE from 2001 to 2010, we find that audit fees are lower for private auditors than those of state auditors. Additionally, the main findings reveal that audit fees decrease as competition increases among auditors. The findings suggest that monopolistic power of the IAO provides an opportunity for the state



auditor to set audit fees which are significantly higher than those of private auditors in the competitive portion of the Iranian audit market. Furthermore, the results show that the negative effect of low demand for high quality audit services can be exacerbated by increased competition in audit market.

The findings of the present study have implications for policy makers. The present study suggests that the monopolistic audit market of the state auditor should be opened up to private audit firms. Such an action can result in equilibrium between the demand and supply sides in the Iranian audit market, which can prevent auditors from obtaining abnormal audit fees (high fees for the state auditor and low fees for private auditors). Additionally, policy makers should provide opportunities for Big 4 audit firms, as high quality auditors, and other international audit firms to operate in Iran. Since clients have the tendency to comply with legal requirements for enforced external auditing by incurring minimum costs, establishing a proper mechanism to determine the minimum rate of audit fees appears to be necessary. When no proper equilibrium exists between the supply side and the demand side, the IACPA should be cautious in allowing for the establishment of new audit firms and should encourage extant private audit firms to merge in order to form medium and large audit firms. The Iranian Parliament should: (i) ratify the modern code of corporate governance to improve the level of investor protection; and (ii) impose pressure on the government to accelerate the market liberalization process of SOEs to shift from an equity-insider system to a market-oriented system. Such fundamental reforms can motivate client firms to demand high quality audit services, while the current low demand for high quality audit services is one of the underlying reasons for aggressive price competition in the Iranian audit market. The suggestions made in relation to policymakers in Iran can also be generalized to regulators in countries with audit markets that are characterized by a weak demand for high quality audit services.

The present study opens a rich avenue for future studies in this domain. The present research only examines the effect of auditor type and audit market competition on audit fees. Hence, future studies can examine the effect of auditor type and audit market competition on other factors, such as audit quality, audit report lag, auditor independence and auditor switching behavior. The descriptive statistics of the present study also reveal that the frequency of the issuance of modified audit opinions is surprisingly high in Iran. Further studies are necessary to determine the underlying cause of this phenomenon in Iran. Since most extant evidence regarding the effect of audit market structure and audit fees are from developed countries, further studies are necessary to investigate this issue in developing countries that have significantly different institutional features than those of developed countries.

The present study is subject to the common limitations of empirical studies of this type. The present study only investigates the effect of auditor type and audit market competition on audit fees in a sample of firms with voluntary audit fees disclosure. As a result, the findings of this study should be interpreted cautiously because the audit pricing behavior of non-disclosed clients can be different. In addition, the sample only contains listed firms on the TSE due to the availability of data. Hence, the findings are less likely to be generalizable to non-listed firms because auditor's pricing strategy can be different for non-listed firms where demand for high quality audit services and litigation risk are lower than those for listed firms.

APPENDIX: VARIABLE DEFINITION

Variables	Definition
<i>Logfee</i>	natural logarithm of total audit fees
<i>Audpvt</i>	1 if auditor is private audit firm, 0 otherwise
<i>HerfNum</i>	modified Herfindahl index based on number of client firms
<i>HerfAsset</i>	modified Herfindahl index based on aggregate size of client firm's assets
<i>HerfSale</i>	modified Herfindahl index based upon client firms' revenues
<i>Opinion</i>	1 if audit opinion is unqualified and 0 for qualified audit opinion
<i>Audchg</i>	1 if auditor switched, 0 if otherwise
<i>Size</i>	is the natural log of a firm's total assets
<i>Lev</i>	total debt divided by the book value of the total assets
<i>InvRec</i>	proportion of inventory and receivables to total assets
<i>Liq</i>	the ratio of total current assets to total current debts



<i>Issue</i>	is a dummy variable equal to 1 if a firm issued common or preferred stocks, 0 if otherwise
<i>ROA</i>	is the return on assets
<i>Loss</i>	a dummy variable that equals 1 when a client has negative net income, and 0 otherwise
<i>Subs</i>	1 if a firm has a subsidiary or subsidiaries, 0 if otherwise
<i>Busy</i>	1 if the fiscal year-end of a firm is 20 March, 0 otherwise
<i>Conown</i>	the per cent of a firm's outstanding shares that are owned by the largest shareholder
<i>NStown</i>	1 if more than 50 per cent of a firm's share owned by private shareholders, 0 if otherwise
<i>SStown</i>	Firms that are not <i>NStown</i> and <i>Stown</i> , but are controlled by state subsidiaries, are coded 1, as semi-state firms
<i>Stown</i>	1 if more than 50 per cent of a firm's share owned by the state, 0 if otherwise
<i>Curr</i>	current assets divided by total assets
<i>Salegrowth</i>	is one-year growth rate in sales
<i>Aturn</i>	asset turnover, computed as sales divided by total assets
<i>AudQual</i>	is absolute discretionary accruals measured by both models developed by Kothari et al. (2005), Ball and Shivakumar (2006) and absolute accrual quality measured by Dechow and Dichev (2002) model
<i>OCF</i>	cash flow from operation deflated by total assets
<i>LogAge</i>	natural log of the number of years from the establishment of a client firm
<i>Disclose</i>	1 if audit fee disclosed and 0 for otherwise
<i>Insown</i>	the per cent of a firm's outstanding shares that are owned by financial institutions
<i>Δ Management</i>	1 if board of directors is changed, 0 if otherwise
<i>IndustryDum</i>	the dummies for 16 industry groups
<i>YearDum</i>	the dummies for fiscal years
ε	error term

REFERENCES

- Al-Harshani, M. O., (2008) "The pricing of audit services: evidence from Kuwait", *Managerial Auditing Journal*, Vol. 23 Iss: 7, pp.685 – 696.
- Anvarkhatibi, S., Safashur, M. and Mohammadi, J. (2012), The effect of auditors opinions on shares prices and returns in Tehran Stock Exchange, *Research Journal of Management Sciences*, Vol. 1(1), 23-27.
- Azizkhani, M. (2011), "Auditor type and earnings quality in Tehran Stock Exchange", *Quarterly Journal of Securities and Exchange*, Vol. 4, No. 16, pp. 229-246.
- Azizkhani, M., Shailer, G. and Monroe, G. (2012), "A competitive pricing of audit services in a non-Big4 market", 13th International Asian Academic Accounting Conference, Kyoto University, Kyoto, Japan. 8-11 November 2012.
- Bagherpour, M., Monroe, G. and Shailer, G. (2008), "Auditor switching in an emerging market for auditor services", AFAANZ/IAAER Conference, Sydney, Australia.
- Bandyopadhyay, S. P., & Kao, J. L. (2001). Competition and Big 6 brand name reputation: Evidence from the Ontario municipal audit market. *Contemporary Accounting Research*, 18(1), 27–64.
- Bandyopadhyay, S.P. and Kao, J.L. (2004), "Market structure and audit fees: A local analysis", *Contemporary Accounting Research*, Vol. 21, No. 3, pp. 529–561.
- Bain, J.S. (1951), "Relation of Profit to Industry Concentration: American Manufacturing 1936-1940." *Quarterly Journal of Economics* 65: 293-324.
- Ball, R., & Shivakumar, L. (2006). The role of accruals in asymmetrically timely gain and loss recognition. *Journal of Accounting Research* 44(2), 207–242.
- Ball, R., S. Jayaraman, and L. Shivakumar, 2012, Audited financial reporting and voluntary disclosure as complements: A test of the Confirmation Hypothesis, *Journal of Accounting and Economics* 53, 136-166.
- Banimahd, B., Noorifard, Y. and Davoudabadi, A. (2013), Auditor-management alignment and audit opinion: Evidence from Iran, *Management Science Letters*, 3, pp.1217–1222.
- Banimahd, B. and Beigi, E., (2012), Audit privatization and opinion shopping: Evidence of Iran, *Interdisciplinary Journal of Contemporary Research in Business*, Vol. 4 (3), 441-449.
- Bedard, J. C., Falsetta, D., Krishnamoorthy, G., & Omer, T. C. (2010). Voluntary disclosure of auditor-provided tax service fees. *Journal of the American Taxation Association*, 32 (1), 59–77.



- Behn, B. K., Lee, J.W. and Jin, L.H. (2009), "An empirical analysis of audit fee price competition after the Korean 1999 Omnibus Cartel Repeal Act", *Journal of International Accounting, Auditing and Taxation*, Vol. 18 No.2, pp.132-140.
- Blankley, A. I., Hurtt, D. N., MacGregor, J. E., 2012. Abnormal audit fees and restatements. *Auditing: A Journal of Practice & Theory* 31(1), 79-96.
- Boone, J.P., Khurana, I.K. & Raman, K.K. 2012. Audit market concentration and auditor tolerance for earnings management. *Contemporary Accounting Research* 29(4): 1171–1203.
- Bozorg Asl. (2010), "The audit quality and fees", *Donya-e-Eqtesad*, 5 March, pp. 17-18 (In Persian).
- Campa, D., 2013, Big 4 fee premium and audit quality: latest evidence from UK listed companies, *Managerial Auditing Journal* 28, 680-707.
- Caneghem, T. V., (2010) "Audit pricing and the Big4 fee premium: evidence from Belgium", *Managerial Auditing Journal*, Vol. 25 Iss: 2, pp.122 – 139.
- Carson, E., Simnett, R., Soo, B.S. and Wright, A.M. (2012), "Changes in audit market competition and the Big N premium", *Auditing: A Journal of Practice & Theory*, Vol. 31 No.3, pp.47-73.
- Chaney, P.K., Jeter, D.C., Shivakumar, L., 2004. Self-selection of auditors and audit pricing in private firms. *The Accounting Review* 79 (1), 51–72.
- Chen, C.J.P., Su, X., Wu, X. (2007), "Market competitiveness and Big 5 pricing: Evidence from China's binary market", *The International Journal of Accounting*, Vol. 42 No.1, pp. 1–24.
- Choi, J., Kim, J., Zang, Y., 2010. Do abnormally high audit fees impair audit quality? *Auditing: A Journal of Practice & Theory* 29 (2), 115–140.
- Datar, S.M., Feltham, G.A. & Hughes, J.S. 1991. The role of audits and audit quality in valuing new issues. *Journal of Accounting and Economics* 14 (1); 3-49.
- Dechow, P., Sloan, R., & Sweeney, A. (1995). Detecting earnings management. *The Accounting Review*, 70, 193–225.
- Dechow, P., & Dichev, I. (2002). The quality of accruals and earnings: the role of accrual estimation errors. *The Accounting Review*, 77, 35–59.
- DeFond, M. L., Wong, T. J., Li, S. H., 2000. The impact of improved auditor independence on audit market concentration in China. *Journal of Accounting and Economics* 28, 269–305.
- DeFond, M. L., Raghunandan, K., Subramanyam, K. R. 2002. Do nonaudit service fees impair auditor independence? Evidence from going-concern audit opinions. *Journal of Accounting Research* 40 (September), 1247–1274.
- Dehkordi, H. J., Makarem, N., 2011. The effect of size and type of auditor on audit quality. *International Research Journal of Finance and Economics* (80), 121-137.
- Deilamipour, M., 2012. A critique for income distribution between audit firms. *Donya-e-Eqtesad*, 10 March: 13 (In Persian, www.donya-e-eqtesad.com).
- Ding, Y. and Jia, Y. (2012), "Auditor mergers, audit quality and audit fees: Evidence from the PricewaterhouseCoopers merger in the UK", *Journal of Accounting and Public Policy*, Vol. 31, pp. 69–85.
- Doa, M., Raghunandan, K., Rama, D. V., 2012. Shareholder voting on auditor selection, audit fees, and audit quality. *The Accounting Review* 87(1), 149–171.
- Esae-Khosh, A. (2011), "Unequal weighing in audit area", *Donya-e-Eqtesad*, 10 October, pp. 21-22 (In Persian).
- Francis, J. R., & Simon, D. T. (1987). A test of audit pricing in the small-client segment of the U.S. audit market. *Accounting Review*, 62, 145–157.
- Francis, J., Wilson, E., 1988. Auditor changes: a joint test of theories relating to agency costs and auditor differentiation. *The Accounting Review*, 663–682.
- Francis, J. R., Wang, D., 2005. Impact of the SEC's public fee disclosure requirement on subsequent period fees and implications for market efficiency. *Auditing: A Journal of Practice & Theory* 24 (Supplement), 145–160.
- Francis, J.R., P. Michas, and S. Seavey, 2013, Does audit market concentration harm the quality of audited earnings? Evidence from audit markets in 42 countries, *Contemporary Accounting Research* 30, 325-355.
- Flint, D., 1988. *Philosophy and Principles of Auditing*. Macmillan Education Ltd, London.



- Ghosh, A., Pawlewicz, R. 2009. The impact of regulation on audit fees: Evidence from the Sarbanes- Oxley Act. *Auditing: A Journal of Practice & Theory* 28 (November), 171–197.
- Gonthier-Besacier, N. & Alain, A., (2007) "Determinants of audit fees for French quoted firms", *Managerial Auditing Journal*, Vol. 22 Iss: 2, pp.139 – 160.
- Government Accountability Office (GAO) (2003), "Public accounting firms: mandated study on consolidation and competition", GAO-03-864, General Accounting Office, available at: www.gao.gov/cgi-bin/gettrpt?GAO-03-864 (accessed in 23 November 2012).
- Gujarati, D., 1995. *Basic econometrics*. McGraw-Hill, Inc.
- Hassas Yeganeh, Y., 2006. Corporate governance in Iran. *Hesabdard* (32), 32-39 (In Persian).
- Hay, D., Knechel, C. R., Wong, N., 2006. Audit fees: A meta-analysis of the effect of supply and demand attributes. *Contemporary Accounting Research* 23 (1), 141–191.
- Heckman, J. J. (1979) Sample Selection Bias as a Specification Error. *Econometrica*, 47, 1, 53-161.
- Hoshi, A., 2012, A concern related to the lack of proper income distribution between auditors, *Donya-e-Eqtesad*, 14 March, 19–20 (In Persian, www.donya-e-eqtesad.com).
- Hovansian Far, G. (2010a), "Forced auditing: Its quality and fees", *Donya-e-Eqtesad*, 26 February, pp.11-12 (In Persian).
- Hovansian Far, G., 2010b, Auditing with very low audit fee, *Donya-e-Eqtesad*, 4 April, 13–14 (In Persian, www.donya-e-eqtesad.com).
- Iran Manesh, M., 2006, Privatization paradox of state owned enterprises, *Cheshm Andaz Iran* 8, 37-40 (in Persian).
- Ivancevich, S.H. and Zardkoohi, A. (2000). An exploratory analysis of the 1989 accounting firm megamergers. *Accounting Horizons*, 14(4), 389–401.
- Iyer, V. and Iyer, G. (1996), "Effect of Big 8 mergers on audit fees: evidence from the United Kingdom", *Auditing*, Vol. 15, pp. 123-132.
- Jensen, K.L. and Payne, J.L. (2005), "The introduction of price competition in municipal audit market", *Auditing: A Journal of Practice & Theory*, Vol. 24 No.2, pp. 137-152.
- Kahana, N., Katz, E., 1990. Monopoly, price discrimination, and rent-seeking. *Journal Public Choice* 64 (1), 94-100.
- Karampinis, N.I. and Hevas, D.L. (2011), "Mandating IFRS in an unfavorable environment: the Greek experience", *The International Journal of Accounting*, Vol. 46, pp. 304–332.
- Kothari, S., Leone, A., & Wasley, C., 2005. Performance matched discretionary accrual measures. *Journal of Accounting and Economics*, 39, 163–197.
- Langbein, L., Wilson, L., 1994. Grounded beefs: monopoly prices, minority business, and the price of hamburgers at U.S. airports. *Public Administration Review* 53 (3), 259-264.
- Larcker, D. F., Richardson, S. A., 2004. Fees paid to audit firms, accrual choices, and corporate governance. *Journal of Accounting Research* 42 (3), 625–658.
- Lawrence, A., M. Minutti-Meza, and P. Zhang, 2011, Can Big 4 versus non-Big 4 differences in audit quality proxies be attributed to client characteristics? *The Accounting Review* 86, 259-286.
- Lennox, C.S. (1999). Non-audit fees, disclosure and audit quality. *The European Accounting Review*, 8 (2), 239–252.
- Lennox, C.S., J.R. Francis, and Z. Wang, 2012, Selection models in accounting research, *The Accounting Review* 87, 589-616.
- Liu, L., Subramaniam, N., 2012. Government ownership, audit firm size and audit pricing: Evidence from China. *Journal of Accounting and Public Policy*, <http://dx.doi.org/10.1016/j.jaccpubpol.2012.11.004>.
- Mahmudi, M. (2010), "Going concern audit report and litigation against auditor", *CPA Journal*, No. 10, pp. 79-87 (In Persian).
- Mashayekhi ,B. and Mashayekh. S. (2008), "Development of accounting in Iran", *The International Journal of Accounting*, Vol. 43, pp. 66-86.
- Menon, K., and Williams. D.D. (2001), "Long-Term Trends in Audit Fees." *Auditing: A Journal of Practice & Theory* 20, 1: 98-136.



- McMeeking, K. P., (2007) "Competition in the UK accounting services market", *Managerial Auditing Journal*, Vol. 22 Iss: 2, pp.197 – 217.
- Mises, L.v. 1998 "Monopoly Prices." *Quarterly Journal of Austrian Economics*, 1 no. 2: 1–28.
- Moayed, V. and Aminfar, M. (2012), "Iran's post-war financial system", *International Journal of Islamic and Middle Eastern Finance and Management*, Vol. 5 No. 3, pp. 264 – 281.
- Mohammadrezaei, F., Saleh, N. M. and Banimahd, B. (2012) "Political economy of corporate governance: The case of Iran", *International Journal of Business, Governance and Ethics*, Vol. 7, No. 4, pp. 301-330.
- Mohammadrezaei, F., Banimahd, B. and Saleh, N. M. (2013), "Convergence obstacles with IASB standards: Evidence from Iran", *International Journal of Disclosure and Governance*, Vol. 10, No. 1, pp. 58-91.
- Niemi, L., 2005. Audit effort and fees under concentrated client ownership: Evidence from four international audit firms. *The International Journal of Accounting* 40, 303– 323.
- Nobes, C.W., 1998. Towards a general model of the reasons for international differences in financial reporting. *Abacus* 34(2), 162–187.
- Numan, W. and Willekens, M. (2012), "An empirical test of spatial competition in the audit market", *Journal of Accounting and Economics*, Vol. 53, pp. 450–465.
- Palmrose, Z.-V. (1986), "Audit fees and auditor size: Further evidence", *Journal of Accounting Research*, Vol. 24, pp. 405–411.
- Pearson, T. and Trompeter, G. (1994), "Competition in the market for audit services: the effect of supplier concentration on audit fees", *Contemporary Accounting Research*, Vol. 11 No. 1, pp. 115–135.
- Rosenbaum, P., and D. Rubin, 1983, The central role of the propensity score in observational studies for causal effects, *Biometrika* 70, 41-55.
- Roudaki, J. (2008), "Accounting profession and evolution of standard setting in Iran", *Journal of Accounting – Business & Management*, Vol. 15, pp. 33-52.
- Schmidt, K., 1997, Managerial incentives and product market competition, *Review of Economic Studies* 64, 191-213.
- Scott, W. D., & Gist, W. E., (2013) "Forced auditor change, industry specialization and audit fees", *Managerial Auditing Journal*, Vol. 28 Iss: 8, pp.708 – 734.
- Shaked A, Sutton J (1982) Relaxing price competition through product differentiation. *Review of Economic Studies*, 49:3–13.
- Simunic, D., 1984. Auditing, consulting, and auditor independence. *Journal of Accounting Research* (Autumn), 679–702.
- Stanley, J. D. (2011) Is the audit fee disclosure a leading indicator of clients' business risk? *Auditing: A Journal of Practice & Theory*, 30(3), pp. 157–179.
- Vafadar Zadeh, A., 2011. The legal responsibilities of auditors. *Donya-e-Eqtesad*, 6 October, 15 (In Persian, www.donya-e-eqtesad.com).
- Whisenant, S., Sankaragurusuvamy, S., Raghunandan, K., 2003. Evidence on the joint determination of audit and nonaudit fees. *Journal of Accounting Research* 41 (4), 721–744.

FAKHRODDIN MOHAMMADREZAEI

Faculty of Economics and Management,

Universiti Kebangsaan Malaysia, 43600 Bangi, Selangor Darul Ehsan, MALAYSIA

fakhroddinmohammadrezaei@yahoo.com,

NORMAN MOHD-SALEH

Faculty of Economics and Management,

Universiti Kebangsaan Malaysia, 43600 Bangi, Selangor Darul Ehsan, MALAYSIA

norman@ukm.edu.my



The Effect of Board Diversity, Multiple Directorships and Ownership Structure on Firm Performance

HASNAH KAMARDIN

School of Accountancy, College of Business

Universiti Utara Malaysia

06010 Sintok, Kedah

MALAYSIA

hasnahk@uum.edu.my

ROHAIDA ABDUL LATIF

School of Accountancy, College of Business

Universiti Utara Malaysia

06010 Sintok, Kedah

MALAYSIA

rohaida@uum.edu.my

KAMARUN NISHAM TAUFIL MOHD

School of Economics, Finance and Banking, College of Business

Universiti Utara Malaysia

06010 Sintok, Kedah

MALAYSIA

kamarun@uum.edu.my

NORIAH CHE ADAM

School of Accountancy, College of Business

Universiti Utara Malaysia

06010 Sintok, Kedah

MALAYSIA

noriah@uum.edu.my

Abstract

The objectives of the study are to examine the effect of some of board of directors' attributes namely board diversity, multiple directorships and ownership structure on firm performance in the Malaysian setting prior to the revised Malaysian Code of Corporate Governance 2012. The study also considers other board attributes commonly studied which are board size, CEO duality and board composition. Samples of the study are Malaysian listed companies on Bursa Malaysia from 2006 to 2010. Firm performance is measured by market to book value (MTBV) and return on assets (ROA). Findings of the study show that higher fraction of either Malay or Chinese directors affect both measures of performance negatively. This suggests that board diversity in terms of ethnicity lead to better performance as diverse board could exploit the strength of ethnically diverse members. Multiple directorships are shown to have positive relationships with both measures of firm performance which support the assumption in 'quality hypothesis'. The results also show that family ownership leads to better accounting



performance but lower MTBV. Finally, even though government linked investment companies (GLIIs) do not influence MTBV, but they are found to lead to better accounting performance. The findings provide supports and implication to the corporate governance policies and practices.

Key Words: Board diversity, multiple directorships, family ownership, government linked investment companies, firm performance, Malaysia.

INTRODUCTION

The effectiveness of non-executive directors is a concern in public listed companies (PLCs) in Malaysia due to the fact that most PLCs have concentrated ownership which shares are owned by blockholders in the hand of management and family. Board of directors (BOD) is an important internal mechanism to monitor managers' performance and to protect shareholders interests. BOD has the mean and power to approve, hire, fire managers while ratify and monitor managers' strategic plan. Malaysian Corporate Governance Blueprint 2011 amplified that good corporate governance are the responsibility of board of directors who act as an active and responsible fiduciaries. It is therefore important to understand the diversity or characteristics of board of directors and how those characteristics can influence the effectiveness of the board. This study is concerned on several characteristics of the board namely board diversity, number of multiple directorships held by directors, board composition, independence of directors, government-link shareholding and directors' shareholding.

Board of directors is assumed to perform various roles, such as providing strategic direction, monitoring executive performances, and building business networking (Wan & Ong, 2005). Within corporate governance structure, non-executive directors have an important position to monitor the management and executive directors (Fama, 1980; Fama & Jensen, 1983). As a check and balance mechanism, outside directors should enhance board's effectiveness. They should bring independence into the board and add to the diversity of skills and expertise of the directors (Abdullah, 2004). They should be able to be business advisers and 'watchdog' to ensure managers act in the interests of outside shareholders. In addition, inside directors, based on their experience working in the same industries, executive and non-independent non-executive directors play important roles to provide effective business strategies to the companies (Carpenter & Westphal, 2001; Kamardin & Haron, 2009).

It is interesting to investigate the influence of ethnicity of board members in relation to firm performance. The strength of each ethnic's culture (Haniffa & Cooke, 2002) would benefit the companies and shareholders. The two dominant ethnics in Malaysia, Malay and Chinese, are examined in this study.

Most studies conducted on multiple directorships focusing on the effectiveness of directors in monitoring and strategic roles. Several studies have suggested that having excessive multiple directorships would have negative implication to firm performance (Haniffa & Hudaib, 2006; Jackling & Johl, 2009), management oversight roles (Kamardin & Haron, 2011b), and strategic roles performed by the directors (Kamardin & Haron, 2009). Despite all the studies above, little knowledge is known about the extent of multiple directorships' practices by different types of directors in public listed companies in Malaysia. This study intends to examine whether multiple directorships by both independent and non-independent directors affect firm performance. Findings of the study related to multiple directorships are expected to explain the extent of such practices by directors.

The concentrated ownership in Malaysia which is controlled by managers and family members might have some implications on the decision making process of the board of directors and consequently on the firm performance. Shareholdings by inside directors (executive directors), family directors would be expected to act as incentives to



work in line with firm performance. The non-linear relationship is expected between executive directors' ownership, family directors' ownership and directors' ownership with firm performance, the entrenchment effect would be expected at the lower percentage of shareholdings and the convergence-of-interest with the outside shareholders would be expected at the higher percentage of shareholdings.

CEO Founder is commonly associated with family controlled firm. Having founder as the CEO (owner-manager), the agency costs associated with managers may be lesser (Fama & Jensen, 1983). Since founder is responsible to initiate the business and firm's early growth, the way the company is governed might be different from others as sustaining the company's growth is crucial to their descendants' future. Thus, it is expected that CEO cum founder would be expected to enhance the firm performance.

The inclusion of new variables in the study such as board diversity in terms of ethnicity of the board members, multiple directorships by type of non-executive directors, family ownership, and government-link ownership which are common to the Malaysian listed companies and different from the western countries' practices would present the actual scenario in Malaysia and other Asian countries. The findings would provide further evidence on the effect of such variables on firm performance.

The objectives of the study are to examine the effect of some of board of directors' attributes namely board diversity in terms of ethnicity, multiple directorships and ownership structure on firm performance in the Malaysian setting prior to the revised Malaysian Code of Corporate Governance 2012. The study also considers other board attributes commonly studied which are board size, CEO duality and board composition. The use of 5-year panel data would provide more interesting and convincing results compared to the cross-sectional data that have been conducted in the previous studies.

LITERATURE REVIEW

1. Ethnicity of the board members

There is limited literature on whether ethnicity influences performance. One of the interesting features of Malaysia is that it is a multi-ethnic nation with Malays, Chinese, and Indians being the major ethnic groups. Total Malaysian population in 2010 is 28.3 million and 67.4 percent of it is Malays, 24.6 percent is Chinese, 7.3 percent is Indians and 0.7 percent others. The strength of each ethnicity may be influenced by their culture. Klitgaard and Katz (1983) reported that back in the 1960s, even though small in number, the Chinese has been stereotyped as highly motivated and hard-working in the economy sector and hold significantly 22.8% of equity interest in Malaysian companies. Most of the Malays in Malaysia are Muslim and according to the Islamic teaching they should be hardworking and trustworthy in all dealings. Consistent with this view, Haniffa and Cooke (2005) and Wan Nordin (2009) find that Malay directors perform better in financial statements disclosures. It is expected that the presence of majority Malay directors would improve the likelihood of detecting financial trouble in time because they are trustworthy and therefore are more transparent in their reporting. The presence of majority Chinese in directorship would reduce the likelihood of firms having lower performance.

Given the limited evidence available pertaining to the relationship between ethnicity and firm performance, it is hypothesized that ethnicity would have an impact on firm performance.

H_1 : There is a relationship between the proportion of Chinese directors and firm performance.

H_2 : There is a relationship between the proportion of Malay directors and firm performance.

2. Multiple directorships

Multiple directorships are common practices in Malaysian PLCs. Kamardin and Haron (2011a) reported that on average 57% of the non-executive directors in a company had at least one additional directorship in other PLCs.



There is an increase percentage compared to the average of 31% reported by Haniffa and Hudaib (2006). Issue on multiple directorships is of concern because pyramidal structure of firms is prevalent in Malaysia. As an example, Yeoh's family owns several public listed firms such as YTL Corporation, YTL Land, YTL Power, YTL Cement, and YTL E-Solution. Therefore, it is possible that family members serve on several boards. To minority shareholders, this might not be at their best interests.

The number of allowable directorships is higher in Malaysia as compared to the U.S.. It is stipulated that the high permissible limit of directorships in Malaysian companies might have some problems for the directors to discharge their roles effectively. Section III of the Bursa Malaysia Practice Note no. 13 and Bursa Listings Requirements allow up to 10 directorships in PLCs and 15 directorships in non-listed firms. In relation to that matter, Minority Shareholders Watchdog Group (MSWG) (2009) has come up with recommendation to limit the directorships of an independent director up to six directorships in Reports on the Corporate Governance and Transparency Index 2009. Comparatively, in the U.S. a director holding less than three multiple directorships is often considered as the best practice. In fact directors holding three or more directorships are considered as "Busy directors" (Ferris et al., 2003; Sarkar & Sarkar, 2009). Recently, the blueprint on corporate governance 2011 recommended that directors can only hold the maximum number of five directorships. The recommendation is based on the study conducted that the majority of directors of both Main and Ace Market have five directorships. The recommendation suggested that multiple directorships have implication on the work of directors. The recommendation is based on the study conducted that the majority of directors of both Main and Ace Market have five directorships. However, the limit for five directorships has been criticized due to the method used to derive at the number is only based on the frequency of directorships. The critic also lies on the matter that it is not really a matter of number which affect significant time commitment but the amount of time and tasks required to make directors add value to the company (Lin See Yan, The Star Online, 3 December 2011).

The effect of multiple directorships can be viewed from two perspectives. The first perspective, *Quality Hypothesis*, views multiple directorships as a proxy for high director quality (Fama, 1980; Fama & Jansen, 1983). Directors with multiple directorships by virtue of more networks are expected to generate benefits by helping to bring in needed resources, suppliers and customers to a company (Booth & Deli, 1996). They would have more experience and knowledge about industry. Directors who have experience in related strategies are expected to be more capable of contributing to strategic decision process (Ruigrok et al., 2006; Carpenter & Westphal, 2001). Several studies have found a positive association between multiple directorships and firm performance (Ferris et al., 2003; Miwa & Ramseyer, 2000; Tan, 2005). Ferris et al. (2003) did not find multiple directors to be associated with a greater likelihood of securities fraud litigation. Mohd Saleh, Mohd Iskandar and Rahmat (2005) show that directors with multiple directorships are effective to detect earnings management. Tan (2005) found multiple directorships to be positively correlated to ownership concentration and to have a positive relationship with firm performance (ROA).

Another perspective, *Busyness Hypothesis*, assumes that directors who serve on multiple boards become so busy that they cannot monitor management adequately, which then leads to high agency costs. Accordingly, directors who serve on multiple boards would be overcommitted and as a consequence, they tend to shirk their responsibilities as directors. Several studies have suggested that having excessive multiple directorships would have negative implication to firm performance (Haniffa & Hudaib, 2006, Jackling & Johl, 2010). Haniffa and Hudaib (2006) found multiple directorships to be negatively related to Tobin's Q and positively related to ROA. The negative relationships are applied to all types of directors. Sarkar and Sarkar (2009) found a negative relationship between "busy" directors (executive directors) and Tobin's Q. A negative relationship is also found for the multiple directorships hold by the non-executive directors (NED) for both ROA and Tobin's Q in India (Jackling & Johl, 2010). A negative relationship is also found with management oversight roles and with strategic roles performed by the directors (Kamardin & Haron, 2011b). Based on previous discussions, the following hypothesis is developed.



H₃: There is a relationship between multiple directorships and firm performance.

3. Inside directors

Inside directors (executive directors) play a vital role in ensuring business performance. The inclusion of executive directors on the BOD poses contradictory issues. On one hand, their inclusion is important and may lead to more effective decision-making process (Fama & Jensen, 1983). Executive directors can effectively assist the CEO to maximise the company's value by providing advice and knowledge about the day-to-day operations. On the other hand, their inclusion invites skepticism as to whether they can be independent enough to judge managerial performance. Rosenstein and Wyatt (1997) found that the market perception on the inclusion of inside directors on BOD is dependent on the level of ownership of each director. The average stock price reaction is significantly negative at low level of directors' ownership which is less than 5%. The market infers that an inclusion of an insider as a director as an attempt to entrench existing administration. The market inferred that director ownership of between 5 to 25% would closely aligned managerial interest to that of the shareholders' and therefore their inclusion on the board would be beneficial. Above 25% inside ownership, the announcement effect is insignificant and is not significantly different from zero. Based on the above argument it is hypothesized that:

H₄: There is a relationship between the proportion of inside directors on the board and firm performance.

4. CEO founder

Founder refers to individual responsible for the firm's early growth and development of the business (Villalonga & Amit, 2006). The number of founder in the company can be more than one person. The presence of a founder in the top management indicates stronger insider commitment and it implies a continuation or extension of the existing strategy. Founder CEO also helps to prevent risks and costs associated with any radical strategic swifts due to leadership change; hence, it provides a valuable signal to outside investors about the firm's current and potential value.

Fama and Jensen (1983) suggest that family relationships among owner-managers should reduce agency costs. Studies on the role of founder are related to the family controlled firms (Chami, 1999; Lee, 2004; McConaughy et al., 1998; Mishra et al., 2001). Family controlled firms are very much governed by family traits which do not exist in non-family controlled firms. Chami (1999) develop a theory of family business which explains the dynamics of family. He shows that family values (e.g. trust and altruism) can create "an atmosphere of love for the business and a sense of commitment". Nepotism and favoritism are held in check by the need for the family business to compete and succeed in the product and capital market. McConaughy et al. (1998) found that both founders and their descendants run their firms more efficiently than CEOs without family ties as founding family firms are characterized by transparent economic conditions and strong social relationship between owners and managers which lead to higher firm performance.

Earlier research on the effects of founder-CEOs on operating performances and market valuations has produced mixed findings. Morck et al. (1988) find that for older firms, there is a negative effect of founding family control on market valuations. For the younger firms in their sample, the market value effect of having a member of the founding family as one of the top two executives is positive. Perez-Gonzalez (2006) finds that inherited control by a family member is associated with a decline in firm performance. In contrast, Sraer and Thesmar (2007) find that family control is positively related to performance, and Villalonga and Amit (2006) find a positive relation between founder-CEOs and firm performance.

Family controlled firms are argued to pursue maximization of sales and shareholder's value well (Thomsen & Pedersen, 2000). Mishra et al. (2001) found a positive association between founding family controlled and firm value, which is consistent with a study in Singapore by Tan et al. (2001). The association between founding family CEOs and firm value is stronger among younger firms and firms with smaller boards. They suggest that founding



family CEOs can enhance firm performance when family influence does not create shareholder entrenchment. In terms of board structure, they found that outside director representation does not improve corporate governance in founding family controlled firms. They argue that "... once the commitment is in place, the need for outside board monitoring is diminished and the inside directors who know the marketplace may be more valuable to these firms ..." (p. 255). In Asian countries, Wiwattanakantang (2001) found controlling shareholder and family controlled firms are associated with higher performance in Thailand. On the other hand, Yermack (1996) found a negative relationship between the presence of a founding family CEO and firm value (Tobin's Q). Based on the conflicting evidence between founders and performance, the following hypothesis is developed:

H₅: There is a relationship between CEO founder and firm performance.

5. Board size

According to resource dependence theory, the increase in the number of board can increase the companies' performance because they can share their expertise, knowledge and experience in the process of decision making (Pfeffer & Salancik, 2003). Uadiale (2010) proposes that companies should have larger board size since larger board can protect companies resources which are limited. Similarly, Dalton, Daily, Johnson and Ellstrand (1999) imply that large board size can increase the performance of companies because they have a connection with the external resources.

However, Jensen (1993) and Yermack (1996) argue that agency problems exist when the size of the board increases as it is difficult to communicate, coordinate and make a decision and it also reduces the capability of the board to manage the organization. Therefore, the existence of the agency costs leads to lower firm performance (Canyon & Peck, 1998). Agency problem in large companies are higher due to the separation of ownership and the process of decision making (Jensen & Meckling, 1976). However, Eisenberg, Sundgren and Wells (1998) reveal that agency problems in small size companies are minimal due to the ownership structure in this type of companies that are closely held. Therefore, the decision to select the size of board is not similar between small and large companies.

Eisenberg, Sundgren and Wells (1998) found that companies' performance which was measured based on profitability (return on assets) have a negative relationship with the size of board. This is consistent with the results of Canyon and Peck (1998) who find a negative relationship between board size in five European countries (UK, France, Netherlands, Denmark and Italy) and return on equity. However, when Tobin's Q is used as a proxy of firm performance, they found a significant negative association only for companies in the UK and the Netherland. In contrast, the insignificant relationship was found for companies in France, Denmark and Italy. They concluded that the negative relationship between the size of the board and companies performance depend on the type of measurement used for company's performance. The result is consistent with a study by Yermack (1996). In addition, a study in Palestine by Daraghma and Alsinawi (2010) also shows a negative association between companies' performance which is measured based on return on revenue or return on sales and the size of the board.

Several studies found a positive relationship between board size and companies' performance. Uadiale (2010) found that larger board can increase the performance of companies as measured by return on equity (ROE) and return on capital employed (ROCE). The result is consistent with studies by Dalton et al. (1999), Dehaene, Vuyst and Ooghe (2001) and Nicholson and Kiel (2003). In Thailand, Yammeesri and Herath (2009) found insignificant relationship between board size and companies' performance. In Malaysia, mixed results are found regarding the relationship between board size and companies' performance. A study by Zainal Abidin, Mustafa Kamal and Jusoff (2009) found a positive relationship; however, Ghazali (2010) did not find any significant relationship between company's performance (using Tobin's Q).

The following hypothesis is developed to test the relationship between board size and firm performance.



H₆: There is a relationship between board size and firm performance.

6. CEO duality

From the agency theory perspective, independent board leadership is necessary to prevent managerial entrenchment. Rechner and Dalton (1991) found that firms with independent governance consistently outperformed the CEO duality firms (one person holds both positions as CEO and Chairman). On the contrary, Wong and Yek (1991) found that CEO duality did not lower the firm value. They argue that the internal incentives (bonus and stock options) and external market system (market for corporate control) have effectively motivated and adequately disciplined management of the firm. Balinga, Moyer and Roa (1996), and Brickley, Coles and Terry (1994) support the claim as their studies found companies with independent board leadership did not show enhanced performance. In Singapore, Wong and Yek (1991) found a significant and positive relationship between CEO duality and modified Tobin's Q. Tan, Chang and Tan (2001) also found CEO duality had positive and significant relationship with Tobin's Q during financial crisis (1997). In Malaysia, Haniffa and Hudaib (2006) found that independent leadership had insignificant relationship to Tobin's Q but had a significant and positive relationship to ROA. Due to mixed results, the present study adopts agency theory because independent board leadership is highly recommended by the MCCG Code. Hence, the following hypotheses are developed.

H₇: There is a negative relationship between CEO duality and firm performance.

7. Director ownership

Directors' ownership provides direct incentives for directors to act in line with shareholders' interests as the wealth of the directors is tied to the performance of the firm (Jensen & Meckling, 1976; Brickley et al., 1988; Weisbach, 1988). Several studies such as Han and Suk (1998), Ang, Cole, and Lin (2000), Filatotchev et al. (2005), Krivogorsky (2006) and Elsayed (2007) find that the presence of larger directors' ownership reduces agency costs and therefore increases performance. However, Mat Nor et al. (2002), Chang (2003), Lin, Huang and Young (2008), and Bathula (2008) find that performance is negatively and significantly related to board ownership. Therefore, the results of the influence of director ownership on performance are mixed.

Morck et al. (1988) found that performance as measured by Tobin's Q increases positively though non-monotonously. Positive relationship to Tobin's Q occurs for managerial ownership of 0% to 5% and beyond 25% while negative relationship occurs for managerial ownership of 5% to 25%. Other empirical evidence on the role of director ownership in reducing agency problem has shown that the relationship between director ownership and firm performance is non-linear (Ruhani & Sanda, 2001; Fauzias et al., 1999; McConnell & Servaes, 1990; Morck et al., 1988; Short & Keasy, 1999; Wong & Yek, 1991). These studies found that at certain level of ownership, managers may get entrenched, which may result in decreased firm performance. Ruhani and Sanda (2001), Chee and Fauziah (2005), and Fauzias et al. (1999) examine the relationship between managerial ownership and firms' performance in Malaysian corporate setting. Fauzias et al. (1999) findings were consistent with those of Morck et al. (1988). Ruhani and Sanda (2001) found higher turning points (curvilinear relationship), positive relation for MOWN less than 36.7% and negative relation when MOWN exceeds 36.7%. Chee and Fauziah (2005) also found a curvilinear relationship but a U-shaped curvilinear. They found positive relation when MOWN is higher which supports the convergence-of-interest hypothesis and is consistent with Morck et al. (1988) and Fauzias et al. (1999). Thus, the hypothesis is:

H₈: There is a relationship between director ownership and firm performance.

8. Family ownership



Family ownership refers to the percentage of shares in a company held by family members (Anderson & Reeb, 2003; Villalonga & Amit, 2006). La Porta et al. (1999) define family controlled firms based on a holding of at least 20% with at least two members are on the board. Chen and Jaggi (2000) and Mishra et al. (2001) use a threshold of 10% to determine family controlled firms. Villalonga and Amit (2006) require that the percentage of shares owned by the founder or a member of the founding family such as an officer, a director, or the owner of at least 5%. Family ownership exceeding certain threshold would qualify it to gain family control over a firm. However, a family can also gain control even having less ownership in a firm. This is achieved through pyramidal structure (La Porta et al., 1999). Thus, family ownership is related to family controlled firms and non-family controlled firms.

Family controlled firms are expected to perform better as the family member(s) could effectively monitor the firm performance and this reduces agency problems (Jensen & Meckling, 1976; Fama & Jensen, 1983; Demsetz & Lehn, 1985; James, 1999; Carney & Gedajlovic, 2002; Joh, 2003). Furthermore, family owners have intimate and superior knowledge about the firm's activities as they have been in contact with the firm since the firm's inception (Kets de Vries 1993). Chami (1999) shows that family values, such as trust, can create a conducive working environment. On the other hand, higher shareholdings could lead family member(s) to take actions that benefit their members at the expense of firm performance. By holding substantial control rights, they could extract private benefits from the firm through excessive compensation, related party transactions, special dividends, and nonpecuniary benefits (Shleifer & Vishny, 1997; DeAngelo & DeAngelo, 2000).

The empirical evidence on the association between performance and family ownership is mixed. Mishra et al. (2001), Wiwattanakantang (2001), Tan, Chang, and Tan (2001), Anderson and Reeb (2003) Filatotchev et al. (2005), Villalonga and Amit (2006), Maury (2006), Martinez, Stohr and Quiroga (2007), Andres (2008), Chu (2009), Saito (2008), Amran and Ahmad (2010) find a positive association between family ownership and firm value while Thomsen and Pedersen (2000), Chang (2003), Chen, Cheung, Stouraitis and Wong (2005), Achmad, Rusmin, Neilson and Tower (2007), King and Santor (2008), Ibrahim and Abdul Samad (2011) and Randoy, Dibrell and Craig (2009) do not find a positive association between performance and family ownership. Thus the following hypothesis is proposed:

H₀: There is a relationship between family ownership and firm performance.

9. Government-linked investment investors (GLIIs)

Many studies find that experienced institutional investors are well equipped on how to manage problem companies. For example, Tykvová, and Borell (2012) find that institutional investors are better able to manage distress risks than their inexperienced counterparts. Furthermore, some institutional owners such as vulture investors are known to be experts in restructuring and turning around companies. These institutional investors may be attracted by firms in financial distress and are likely to increase their ownership positions to profit from distress situations.

Studies on the relationship between government-linked investment companies (GLICs) and firm performance have found that these two variables are positively related (Abd. Razak, Ahmad & Aliahmed, 2008; Lau & Tong, 2008; Le & Buck, 2009; Zeitun & Yian, 2007). These studies find that when companies are controlled by government-linked investment companies, the performance of the companies is generally good, and hence the companies would not suffer from financial distress. Since the objective of GLICs is to hold the investment for a longer period, it is expected that GLICs would monitor the firms that they controlled. Institutional investors are choosy in selecting their investments and only invest in good performing firms.

However, there are also studies such as those by Gunasekarage, Hess and Hu (2007), Peng (2004), and Wei, Xie and Zhang (2005) report government-linked investment companies are negatively related to the performance of the firm. Thomson and Pederson (2000), who study the impact of ownership structure on company performance in



Continental Europe, find that government ownership is negatively related to performance as measured by market-to-book ratio and return on assets. It is hypothesized that:

H₁₀: There is a relationship between the ownership of government-linked investment investors and firm performance.

10. Foreign ownership

To mitigate agency problems between controlling and minority shareholder, existence of foreign investors could be a good corporate governance mechanism as it reduces opportunistic behavior of the controlling shareholders. There is mixed evidence on the effect of foreign ownership on performance. A number of studies indicate that the existence of foreign owners bring about positive impact on performance (see for example, Boyer & Zheng, 2009; Douma, George & Kabir, 2006; Che-Haat, Rahman & Mahenthiran, 2009; Makhija & Spiro, 2000; Piesse, Filatotchev & Lien, 2007; Tian & Estrin, 2008). It is demonstrated that the higher is the percentage of ownership owned by foreigners, the better would be the performance of the company, hence the lower the likelihood that the company would become bankrupt. For example, Makhija and Spiro (2000) find that the share prices of newly privatized Czech firms are positively related to the existence of foreign investor proportion. Likewise, a study by Che-Haat, Abdul Rahman, and Mahenthiran (2008) indicates that foreign ownership has strong predictive power on firm performance in Malaysia.

Generally, previous studies found that foreign investors would favor to invest in country with strong investor protection law and in firms that have strong financial performance, large cash positions and high dividend payout (see for example, Baba, 2009; Lin & Shiu, 2003; Dahlquist & Robertsson, 2001). On the contrary, Omran, Bolbol, and Fatheldin (2008) find no support that the existence of foreign ownership affects performance of firms in Egypt, Jordan, Tunisia and Oman. Based on the literature review, it is expected that foreign investors would be likely to invest in good performance companies and would bail out their position in case of financial difficulties. It is hypothesized that foreign investors are selective in their investment companies and are capable of predicting firm performance. Therefore our next hypothesis is:

H₁₁: There is a relationship between foreign ownership and firm performance.

METHODOLOGY

1. Sources of data

Population of the study is companies listed on the Bursa Malaysia from 2006 to 2010, for both Main Board and Second Board. Starting from September 2009, Main Board and Second Board are merged to form Main Market. Sample firms are selected from a list of 943 companies listed on the Main Market in 2006. Using stratified systematic sampling, 20 percent of these companies are chosen as sample firms. All PN17 companies (distressed firms), REITS, closed-end funds, exchange traded funds and financial institutions are excluded from the sample as these companies are subjected to different requirements and rulings. Companies with missing data on market to book value (MTBV) are also excluded. These processes produced 183 unique companies with 836 firm-year observations. Table 1 summarizes the industrial classification of the companies.

TABLE 1: Sample companies based on Bursa Malaysia industry classification

Industry	frequency	Percentage (%)
1 Construction	13	7.10
2 Consumer	28	15.30



3	Industrial	55	30.05
4	IPC and mining	3	1.64
5	Plantation	7	3.83
6	Property	21	11.48
7	Technology	26	14.21
8	Trading & services	30	16.39
Total		183	100.00

Corporate governance and ownership structure data are gathered from the annual reports available from Bursa Malaysia website while data on company financial characteristics are taken from the DataStream database. Only directorships in the public listed companies are considered in this study. This is due to the Bursa Malaysia Listing Requirement to disclose only multiple directorships in public listed companies. In addition, not all companies voluntarily disclose directorships in private companies. Detail data on the directorships are gathered from the director profile of each individual director in a company. Data are then classified into different type of directors.

2. Model of the study

To investigate the relationship between corporate governance mechanisms and performance of companies, three models are estimated:

$$\text{Model 1: } Y_{it} = \alpha_0 + \alpha_1 \text{FRACMALAY}_{it} + \alpha_2 \text{FRACCHINESE}_{it} + \alpha_3 \text{LNMULTIDIR}_{it} + \alpha_4 \text{FRACINSIDERS}_{it} + \alpha_5 \text{CEOFOUNDER}_{it} + \alpha_6 \text{BOARDSIZE}_{it} + \alpha_7 \text{DUAL}_{it} + \alpha_8 \text{BOARDOSHIP}_{it} + \alpha_9 \text{FAMILYOWN}_{it} + \alpha_{10} \text{TOTALGLIIS}_{it} + \alpha_{11} \text{FOREIGN}_{it} + \sum Z_{it} * b$$

Where i refers to company, t refers to year.

Y	Performance of company i in year t measured by market to book value (MTBV) and return on assets (ROA)
FRACCHINESE	Proportion of Chinese directors to total directors
FRACMALAY	Proportion of Malay directors to total directors
LNMULTIDIR	Natural logarithm of multiple directorships held by directors
FRACINSIDERS	Proportion of inside directors to total directors
CEOFOUNDER	A binary variable that equals to “1” if the CEO is also the founder, “0” otherwise
BOARDSIZE	The number of directors
DUAL	A binary variable that equals to “1” if the CEO is also the chairman, “0” otherwise
BOARDOSHIP	Proportion of shares held by all directors
FAMILYOWNSHIP	Proportion of shares held by a family
TOTALGLIIS	Proportion of shares held by government-linked institutional investors
FOREIGN	Proportion of shares held by foreigners
Z	Control variables, i.e., leverage, market return, lagged of market return, and GDP growth



$$\text{Model 2: } Y_{it} = \beta_0 + \beta_1 \text{FRACMALAY}_{it} + \beta_2 \text{FRACCHINESE}_{it} + \beta_3 \text{MDINDDIR}_{it} + \beta_4 \text{MDEXECDIR}_{it} + \beta_5 \text{FRACINSIDERS}_{it} + \beta_6 \text{BOARDSIZE}_{it} + \beta_7 \text{DUAL}_{it} + \beta_8 \text{CEOFOUNDER}_{it} + \beta_9 \text{BOARDOSHIP}_{it} + \beta_{10} \text{FAMILYOWN}_{it} + \beta_{11} \text{TOTALGLIIS}_{it} + \beta_{12} \text{FOREIGN}_{it} + \sum Z_{it} * b$$

Where:

MDINDDIR	Average multiple directorships held by independent directors
MDEXECDIR	Average multiple directorships held by executive directors

The other variables have been defined in Model 1.

Model 2 aims to test if multiple directorships by independent and executive directors have different effects on performance. Directors who serve on several boards might be less effective in running their company as they might be busy. However, if by serving several boards increased their connections and experience, a positive relationship between directorships and performance could be expected. In this case the signs of β_3 and β_4 cannot be determined.

It could be argued that by sitting on several boards, a director could build more connections and gain more experience but as the number of directorships increased, so will be the director's 'busyness'. In this case, a nonlinear relationship might be more appropriate. Thus, Model 3 takes into account the non-linear relationship between multiple directorships and performance.

$$\text{Model 3: } Y_{it} = \delta_0 + \delta_1 \text{FRACMALAY}_{it} + \delta_2 \text{FRACCHINESE}_{it} + \delta_3 \text{MDINDDIR}_{it} + \delta_4 \text{MDINDDIR}_{it}^2 + \delta_5 \text{MDEXECDIR}_{it} + \delta_6 \text{MDEXECDIR}_{it}^2 + \delta_7 \text{FRACINSIDERS}_{it} + \delta_8 \text{CEOFOUNDER}_{it} + \delta_9 \text{BOARDSIZE}_{it} + \delta_{10} \text{DUAL}_{it} + \delta_{11} \text{BOARDOSHIP}_{it} + \delta_{12} \text{FAMILYOWN}_{it} + \delta_{13} \text{TOTALGLIIS}_{it} + \delta_{14} \text{FOREIGN}_{it} + \sum Z_{it} * b$$

Where:

MDINDDIR_{it}^2	Square of average multiple directorships held by independent directors
MDEXECDIR_{it}^2	Square of average multiple directorships held by executive directors

The other variables have been defined in Model 1.

EMPIRICAL RESULTS

1. Descriptive analysis

Table 2 summarizes statistics of variables: companies' characteristics, board and directorships. Multiple directorships are determined by using three measures: a) natural log of total multiple directorship (LNMULTIDIR) b) average multiple directorship of the executive directors (MDEXECDIR), and c) average multiple directorship of the independent directors (MDINDDIR). The average and median for the total number of multiple directorships (MULTIDIR) are 13.95 and 12 respectively. On average (AVEMULTIDIR), all directors in the sample firms hold directorship in two companies concurrently. This number is in tandem with the recommended number of directorship as prescribed by the Malaysian code on corporate governance 2012. It is clear from Table 2 that the average number of multiple directorships by independent directors (MDINDDIR) is about 2 and is higher compared to average number of directorships by executive directors (MDEXECDIR), which is 1.47. Based on 836 firm-year



observations, the average board size (BOARDSIZE) is 7.1 with a minimum of 3 members and a maximum of 13 members. Directors can be classified based on function and independence: a) executive or inside directors, b) independent directors and, c) non-independent and non-executive directors (NINE) or gray directors. The mean and median of executive directors (INSIDER) on companies' board is 2.76 and 3 respectively. These executive directors (FRACINSIDER) made up about 40 percent of directors.

TABLE 2: Descriptive analysis of variables

Variables	Mean	Median	Std. Deviation	Minimum	Maximum
MULTIDIR	13.953	12.000	7.277	4.000	50.000
LNMULTIDIR	2.522	2.485	0.467	1.386	3.912
AVEMULTIDIR	1.967	1.714	0.913	0.909	5.857
MDEXECDIR	1.468	1.000	0.987	0.000	7.000
MDINDDIR	2.302	2.000	1.301	0.000	7.000
BOARDSIZE	7.124	7.000	1.695	3.000	13.000
INSIDER	2.760	3.000	1.466	0.000	9.000
FRACINSIDER	0.388	0.400	0.173	0.000	0.800
DUAL	0.102	0.000	0.302	0.000	1.000
CEOFOUNDER	0.167	0.000	0.374	0.000	1.000
MALAYDIR	2.420	2.000	2.077	0.000	11.000
FRACMALAY	0.336	0.286	0.270	0.000	1.000
CHINESEDIR	4.347	5.000	2.344	0.000	11.000
FRACCHINESE	0.613	0.667	0.298	0.000	1.000
FAMILYSHIP	26.051	27.170	23.547	0.000	79.280
BOARDOSHIP	36.348	37.580	21.740	0.000	79.280
TOTALGLIIS	4.336	0.000	10.196	0.000	81.000
FOREIGN	5.562	1.155	10.578	0.000	69.950
TOTAL ASSETS ('000)	804,086	205,300	2,715,935	13	36,637,299
TOTAL DEBT ('000)	250,035	33,538	1,436,050	0	21,243,063
LEVERAGE	0.223	0.188	0.407	0.000	1.898
GDP	0.045	0.056	0.031	-0.015	0.074
MTBV	1.151	0.740	2.478	-15.340	33.220
ROA	1.475	3.820	17.876	-299.060	56.960
ROE	-4.999	5.325	132.046	-3541.620	215.700

To investigate the incidence of CEO duality and CEO founder, dummy variables are used. Analysis of the data indicates that 17 percent (140 out of 836 observations) of the sample companies have CEO who is also the chairman of the board while only 10 percent (86 out of 836 observations) of the sample companies still have their founder effectively running the company. For ethnic diversity on board of directors among sample firms, it is found that the median percentage of Chinese directors is 67 percent,



followed by Malay directors of 29 percent, thus the remaining 4 percent of directors come from Indian and other minority groups.

Family-controlled companies are dominant in Malaysia. This study measures family controlled companies as an individual or a family holding at least 10 percent of the shares outstanding and that individual or the representative of that family serves on the board of directors²¹. The average and maximum family ownership (FAMILYOSHIP) is 26 percent and 79 percent respectively. Bursa Malaysia Listings requires that the public shareholdings spread should be at least 25 percent. The result of this study shows that the maximum ownership is greater than the allowed percentage as Metacorp Bhd has family ownership of more than 79 percent in 2008. Ownership by directors (BOARDOSHIP) is high in Malaysia as the average (median) value is 36.35 percent (37.58 percent). Detailed analysis of the data indicates that 474 out of 836 observations or 57 percent of the sample have government-linked investment companies (TOTALGLIIS) holding between 0.1 percent and 81 percent. The average holding for all 836 observations by government-linked investment companies is 4.336 percent. Foreign ownership is a little bit higher as foreigners own 5.562 percent of shares outstanding.

The average size of the sample companies as measured by total assets in 2006 to 2010 is RM 804,086,000. On average, sample firms have total debts of RM 250,035,000 or low average gearing ratio of 23 percent. The maximum level of leverage is nearly 190 percent and this value is driven by three dead companies, Intelligent Edge Technologies Berhad, Rimbunan Sawit Berhad and Wonderful Wire and Cable Berhad. Although the mean performance on MTBV is considered normal (1.51), the minimum and maximum values can be considered as extreme cases (minimum value of -15.34 while maximum value is 33.22). Likewise, there are extreme values for ROA which indicate the existence of outliers. Therefore, these values will be adjusted accordingly to mitigate the problems associated with outliers.

2. Correlation analysis

Before conducting the regression analysis, the relevant variables are tested for correlation and heteroskedasticity. Pearson pair-wise correlations are evaluated between explanatory variables and the results are presented in Table 3. None of the correlations is greater than 0.5 except for the correlations between average multiple directorship by independent directors (MDINDDIR) and natural log of multiple directorship (LNMULTIDIR), family ownership and board ownership, fraction of Malay directors and fraction of Chinese directors, and GDP and lag market return. The high correlations raise concerns on possible multicollinearity problems. However, variance inflation factors (VIF) do not give values greater than 10, which show that multicollinearity is not a problem.

²¹ In the subsequent regression analyses, cutoff points of 20% and 2 family members are also used but the results do not change.



TABLE 3: Correlation matrixes between explanatory variables

	LNBOARDSIZE	LNMDIR	FRACINSIDERS	MDEXECDIR	MDINDDIR	DUAL	CEFOUNDER	BOARDOSHIP	FAMILYOWN	TOTALGLIIS	FOREIGN	FRACMALAY	FRACCHINESE	MKTRTNCOMP	LMKTRTN	GDP	LEVERAGE
LNBOARDSIZE																	
LNMDIR	.477*																
FRACINSIDERS	-.012	-.312*															
MDEXECDIR	-.020	.409*	-.070														
MDINDDIR	-.019	.652*	-.185*	.110*													
DUAL	-.17*	-.238*	.176*	-.093*	-.125*												
CEFOUNDER	.066	-.054	.189*	-.014	-.099*	.231*											
BOARDOSHIP	.125*	-.137*	.298*	-.066	-.177*	.090	.235*										
FAMILYOWN	.075	-.048	.209*	.062	-.039	-.104*	.176*	.639*									
TOTALGLIIS	.250*	.304*	-.242*	-.009	.135*	-.101*	-.062	-.252*	-.121*								
FOREIGN	.036	.178*	-.166*	.094*	.232*	-.069	-.082	-.216*	-.121*	.074							
FRACMALAY	.043	.381*	-.378*	.203*	.239*	-.131*	-.110*	-.277*	-.224*	.293*	.010						
FRACCHINESE	-.074	-.371*	.373*	-.180*	-.244*	.111*	.150*	.311*	.240*	-.284*	-.138*	-.870*					
MKTRTNCOMP	.002	.013	.010	.007	.000	-.019	-.003	-.017	-.003	-.003	.001	-.001	-.019				
LMKTRTN	-.007	-.014	-.001	-.011	-.011	.017	.015	.008	-.001	.000	-.012	-.004	.017	-.561*			
GDP	-.010	-.007	.026	-.002	.000	.005	.013	.013	.017	.027	.001	.019	-.003	-.317*	.886*		
LEVERAGE	-.09*	.056	-.023	.181*	.066	-.071	-.059	-.096*	.018	-.061	.061	.066	-.087	-.046	-.006	-.019	

*Denotes significance at 1% (2-tailed)



3. Results of regression analyses

Table 4 reports the results of regression analyses for the full sample of 836 firm-years where performance is measured using market-to-book value ratio. Breusch-Pagan test is carried out to test for heteroscedasticity. As the value of Breusch-Pagan is significant at 1% level for all regression models, standard errors are corrected for heteroscedasticity. The second column of Table 4, or Model 1a, shows that the ratio of either Malay or Chinese directors to total directors, FRACMALAY and FRACCHINESE respectively, lead to lower performance as compared to other ethnicities. This finding supports the argument that board of directors must be diverse. Diversity in the board would lead to better decision making.

Multiple directorships, as measured by the natural logarithm of total directorships in listed companies or LNMULTIDIR, have a significant positive impact on performance. The significant positive effect of multiple directorships shows that the benefits of “quality” hypothesis outweigh the costs of “busyness” hypothesis. By serving in multiple boards, directors bring along their experience to boardroom discussions and their networking connections could be utilized by the company. These lead to better decision making and higher firm performance. Furthermore, the performance of listed companies is followed by investors and the performance could affect the reputation of the directors. Thus the greater is the number of directors, the better is the performance of the firm. The significant positive result of multiple directorships is in contrast to that of Haniffa and Hudaib (2006) who find a negative relationship between multiple directorships and MTBV in Malaysia. However, the finding is consistent with the finding of Sarkar and Sarkar (2009).

Mat Nor et al. (2002) and Haniffa and Hudaib (2006) report that performance is positively related to board size while Ibrahim and Abdul Samad (2011) find that firm performance is negatively related to board size. This study finds that board size is not significant in explaining performance. This finding shows that a company would choose a board size where the benefits of both large and small boards could be realized.

TABLE 4: Results of regression analyses based on MTBV

Variables	Model 1a	Model 1b	Model 2a	Model 2b	Model 3a	Model 3b
LNMULTIDIR	0.618**	0.640***				
MDINDDIR			0.334**	0.332**	-0.682	-0.677
SQMDINDDIR					0.165*	0.164*
MDEXECDIR			-0.113*	-0.132**	-0.237	-0.244
SQMDEXECDIR					0.017	0.016
BOARDSIZE	0.032		0.081		0.085*	0.082*
FRACINSIDERS	1.053*	0.992*	0.909*	0.908	0.935*	0.960*
FRACMALAY	-3.135**	-3.256***	-3.018**	-3.062***	-2.912***	-2.947***
FRACCHINESE	-2.654**	-2.792***	-2.619**	-2.674***	-2.635***	-2.624***
DUAL	-0.042		-0.061		-0.085	
CEOFOUNDER	0.088		0.138	0.167*	0.206*	0.204*
FAMILYOWN	-0.006*	-0.009**	-0.006*	-0.007**	-0.006*	-0.006**
BOARDOSHIP	-0.007		-0.006	-0.004	-0.007	-0.006
TOTALGLIIS	-0.005		-0.006		-0.006	
FOREIGN	0.006		0.002		0.003	
LEVERAGE	-0.666**	-0.601	-0.573		-0.554	
MKTRTN	0.089		0.131		0.156	
LAGMKTRTN	-0.315		-0.269		-0.283	



GDP	6.483		6.220		6.355	
CONSTANT	2.077**	2.339***	2.480***	3.190***	3.738***	3.863***
R-squared	0.059	0.053	0.078	0.070	0.099	0.093
F-statistic	2.45	5.03	2.13	1.82	1.96	1.55
(p-value)	(0.002)	(0.000)	(0.006)	(0.069)	(0.010)	(0.109)

Note: ***, **, * Significance at 1%, 5% and 10% respectively.

The ratio of executive to total directors (FRACINSIDERS) is marginally significant in determining performance. This finding shows that a larger number of executives on board would lead to better decision making as they are more knowledgeable in day-to-day operations of the companies. Even though they might be more inclined to take actions that benefit their self-interest to the detriment of other shareholders, that opportunistic behavior is not evident in this study.

CEO-duality, where a CEO also serves as a chairman, does not influence performance. Duality could lead to more power for CEOs. Hence, it could lead to lower performance if CEOs use that power to increase their well-being. However, in a concentrated ownership environment like Malaysia, CEOs themselves might hold a large stake in their companies. Thus, they will not take any action that could reduce their firms' performance as their wealth is closely linked to the performance of their firms.

Since founders tend to possess stronger economic connection and psychological attachment to their companies, as they owned considerable amount of shares and they put more effort to make sure that their companies succeed, it is expected that by serving as CEOs, they could increase the performance of their companies. However, the finding does not support that hypothesis. A possible reason is that even though they are motivated to work hard, their judgments could be clouded by emotional attachments.

Family ownership, FAMILYOWN, influences performance negatively. It seems that investors expect that higher shareholdings by families could lead family members to take actions that benefit their members at the expense of firm performance. By holding substantial control rights, they could extract private benefits from the firm through excessive compensation, related party transactions, and non-pecuniary benefits.

Ownerships by directors (BOARDOSHIP), government-linked investment companies (TOTALGLIIS) and foreigners (FOREIGN) do not influence performance. As for the control variables, only leverage (ADJLEVER) is significant. Higher leverage leads to lower performance. Market return (MKTRTN), lag of market return (LAGMKTRTN) and GDP do not influence performance.

In Model 1b, insignificant variables as identified through F-tests are dropped. The results of Model 1b in column three of Table 4 reflect those of Model 1a. Model 2a, in column four of Table 4, divided multiple directorships based on directors' types. MDINDDIR refers to multiple directorships by independent directors while MDEXECDIR refers to multiple directorships by executive directors. It shows that higher directorships by independent directors lead to better performance, which supports "quality" hypothesis while higher directorships by executive directors lead to lower performance, which supports "busyness" hypothesis. The results are more significant in Model 2b in column five after insignificant variables are dropped. Model 3a and its reduced form Model 3b show that multiple directorships by independent and executive directors do not follow non-linear relationship.



Results in Table 4 look at the whole sample without adjusting for outliers of the dependent variable (MTBV). Table 5 summarizes the results after adjusting for outliers for MTBV where outliers are identified either by using three-standard-deviation approach or fixed percentage approach. The values of the outliers based on three-standard-deviation approach then would take on the values of mean plus or minus three standard deviations. As an example, if the value of mean plus three standard deviations is 8.58, then observations with MTBV greater than 8.58 will take on the value of 8.58. Similar steps are taken for observations with MTBV smaller than mean minus three standard deviations. Under fixed percentage approach, where 0.5% is used as the percentage, 0.5% of total observations (826 firm-years) or four firms with the highest and lowest MTBVs will take on the value of the fifth highest and fifth lowest MTBV values respectively.

Models 1 and 2 summarize the results of using fixed percentage approach to identify the outliers while Models 3 and 4 use three-standard-deviation approach. Models 1 and 3 present the results when the natural logarithm of multiple directorships are used while Models 2 and 4 present the results when total multiple directorship are broken down into multiple directorships by independent directors and executive directors. The results in Table 5 are basically similar to results of Table 4 with one notable exception where the coefficients of multiple directorships by executive directors are not significant anymore.

TABLE 5: Results of regression analyses after adjusting for outliers

Variables	Model 1: MTBV (0.5%)	Model 2: MTBV (0.5%)	Model 3: MTBV (3SD)	Model 4: MTBV (3SD)
LNMULTIDIR	0.559***		0.294***	
MDINDDIR		0.272**		0.114**
SQMDINDDIR				
MDEXECDIR		-0.079		-0.023
SQMDEXECDIR				
BOARDSIZE				
FRACINSIDERS	0.971**	0.874**	0.504*	0.430
FRACMALAY	-2.649***	-2.501***	-1.381***	-1.304***
FRACCHINESE	-2.262***	-2.227***	-1.249***	-1.246***
DUAL				
CEOFOUNDER				
FAMILYOWN	-0.009**	-0.008**	-0.003	-0.003
BOARDOSHIP				
TOTALGLIIS				
FOREIGN				
LEVERAGE	-0.533*	-0.522*	-0.898***	-0.897***
MKTRTN				
LAGMKTRTN				
GDP				
CONSTANT	1.978***	2.820***	1.622***	2.125***
R-squared	0.059	0.075	0.063	0.066
F-statistic (p-value)	5.67 (0.000)	4.61 (0.000)	5.94 (0.000)	5.02 (0.000)

Note: ***, **, * Significance at 1%, 5% and 10% respectively.



To investigate whether the results based on market valuation still hold for accounting based valuations, regressions are estimated using ROA as dependent variable. Table 6 presents the results based on ROA. Model 1a is the full model using natural logarithm of multiple directorships while the rest of the models report only significant variables. Table 6 shows that multiple directorships are significant in explaining ROA at 1%-level either for full Model 1a or restricted Model 1b. Fraction of Malay directors (FRACMALAY) is not significant while fraction of Chinese directors (FRACCHINESES) is marginally significant in Models 1a, 1b and 2. Again this finding shows that a firm gains if its directors serve as directors of other firms, which supports 'quality' hypothesis. When multiple directorships are separated into multiple directorships by independent and executive directors, both coefficients are positively significant as summarized by Model 2. Unlike the results based on MTBV where family ownership (FAMILYOWN) leads to lower performance, Table 6 shows that family ownership influences ROA positively. Furthermore, ownership by directors (BOARDOSHIP) and government-linked investment companies (TOTALGLIIS) also lead to higher ROA. If outliers are adjusted, the above results still hold except that multiple directorships by independent directors do not influence ROA and FRACMALAY negatively influences ROA, as reported as reported in Models 3 to 6.

TABLE 6: Results of regression analyses based on ROA

Variables	Model 1a	Model 1b	Model 2	Model 3 ROA 0.5%	Model 4 ROA 0.5%	Model 5 ROA 3SD	Model 6 ROA 3SD
LNMULTIDIR	6.174***	5.498***		3.847***		3.561***	
MDINDDIR			1.054*		0.687		0.614
SQMDINDDIR							
MDEXECDIR			1.849**		1.099**		0.778*
SQMDEXECDIR							
FRACINSIDERS	9.272*	9.341*	7.483				
FAMILYOWN	0.073***	0.108***	0.064**	0.089***	0.050**	0.091***	0.075***
FRACMALAY	-7.862	-6.789	-7.548	-10.576***	-11.048***	-11.134***	-11.201***
FRACCHINESE	-6.846*	-6.078*	-7.068*	-7.749***	-8.785***	-8.181***	-8.693***
DUAL	-2.369		-2.527*		-2.975**		-2.468*
CEOFOUNDER	1.269			1.609*	1.989**	1.785**	2.395***
BOARDOSHIP	0.055*		0.068**		0.056**		0.068**
BOARDSIZE	-3.851						
LEVERAGE	-27.887***	-27.902***	-28.578***	-17.866***	-18.162***	-14.495***	-15.063***
TOTALGLIIS	0.111***	0.085**	0.152***	0.0798**	0.127***	0.079***	0.106***
FOREIGN	0.025						
MKTRTN	-0.851						
LAGMKTRTN	-4.648						
GDP	35.981						
CONSTANT	-2.405	-6.078*	2.379	1.741	8.088***	2.519	9.594***
R-squared	0.181	0.176	0.178	0.1625	0.165	0.143	0.140
F-statistic (p-value)	5.70 (0.000)	7.88 (0.000)	6.25 (0.000)	11.28 (0.000)	9.14 (0.000)	13.58 (0.000)	11.40 (0.000)

Note: ***, **, * Significance at 1%, 5% and 10% respectively.



CONCLUSION

Results on the relationships between performance measures (MTBV and ROA) indicate that higher fraction of either Malay or Chinese directors affect all measures of performance negatively. This means that board diversity in term of ethnicity lead to better performance as diverse board could exploit the strength of ethnically diverse members.

This study also contributes to the literature by documenting the the extent of multiple directorship practices among public listed companies in Malaysia. This study documents that on average, companies in Malaysia have big board of directors typically consists of 7 members. On average, these directors held another directorship in a public listed company and the maximum number of directorships in public listed companies is 6. Therefore it can be concluded that multiple directorship is not alarming in Malaysian business environment. In addition, multiple directorships do not lead to deteriorating performance. In fact, multiple directorships may lead to better performance. This indicates that multiple directorships in Malaysia enhance the effectiveness of advising, monitoring, and controlling functions of directors. The result seems to suggest that multiple directorships could provide better business networking, reduced competition as the directors serve multiple companies, or increased synergies in the forms of additional insights or expertise.

Furthermore, this study finds that total multiple directorships must be segregated based on types of directors to better assess performance. Multiple directorships by independent directors are found to lead to better performance as measured by MTBV and ROA while multiple directorships by executive directors lead to better performance if ROA is used but poor performance if MTBV is used. The results suggest that investors prefer 'busy' independent directors but not 'busy' executive directors.

This study also finds that family ownership leads to better accounting performance but lower MTBV. Lower MTBV could be due to the fact that family might unduly use resources of its controlled company. Finally, even though government linked investment companies (GLIIs) do not influence MTBV, they lead to better accounting performance.

Our study complements several other studies examining the effectiveness of directors monitoring role in a concentrated environment (see for example, Andres & Vallelado, 2008; Haniffa & Hudaib, 2006; Ismail & Abdul Rahman, 2011).

A limitation of this study is that it is based on a sample of 20 percent of the population. Thus, there might be a possibility that the sample is biased even though random sampling is used. The study can be extended in several ways. First, the result can be differentiated better if the effects of industry are controlled. It is also argued that the relationship between family ownership and performance is not linear. Thus, robust analysis can be conducted to enhance our understanding on the nature of the relationships.

References:

- Abdullah, Shamsul-Nahar (2004). Board composition, CEO duality and performance among Malaysian listed companies. *Corporate Governance*, 4(4), 47-61.
- Ab Razak, N. H., Ahmad, R., & Aliahmed, H. J. (2008). Ownership structure and corporate performance: A comparative analysis of government linked and non-government linked companies from Bursa Malaysia. Working Paper, Electronic copy available at: <http://ssrn.com/abstract=1252502>



- Achmad, T., Rusmin, Neilson, J. & Tower, G. (2007) The iniquitous influence of family ownership structures on corporate performance, *The Journal of Global Business Issues*, 3(1), 41-48.
- Amran, N. A. & Ahmad, A. C. (2010). Corporate governance mechanisms and performance: Analysis of Malaysian family and non-family controlled companies. *Journal of Modern Accounting and Auditing*, 6(2), 1-15.
- Anderson, R.C., & Reeb, D.M. (2003). Founding-family ownership and firm performance: evidence from the S&P 500. *Journal of Finance* 58: 1301-1328.
- Andres, C. (2008). Large shareholders and firm performance: An empirical examination of founding-family ownership. *Journal of Corporate Finance* 14: 431-445.
- Andres de P., & Vallelado, E. (2008). Corporate governance in banking: The role of the board of directors. *Journal of Banking & Finance*, 32, 2570-2580.
- Ang, J., Cole, R., & Lin, J. (2000). Agency costs and ownership structure, *Journal of Finance*, 55: 81-106.
- Baba, N. (2009). Increased presence of foreign investors and dividend policy of Japanese firms, *Pacific-Basin Finance Journal*, 17, pp. 163-174.
- Balinga, B. R., Moyer, R.C., & Rao, R.S. (1996). CEO duality and firm performance: What's the fuss? *Strategic Management Journal*, 17(1),41-43.
- Bathula, H. (2008). Board characteristics and firm performance: Evidence from New Zealand. *PhD thesis submitted to Auckland University of Technology*.
- Booth, J. R., & Deli, D. N. (1996). Factors affecting the number of outside directorships held by CEOs. *Journal of Financial Economics*, 40(1), 81-104.
- Boyer, B. & Zheng, L. (2009). Investor flows and stock market returns. *Journal of Empirical Finance*, 16, 87-100.
- Brickley, J.A., Coles, J.L. & Terry, R. L. (1994). Outside directors and the adoption of poison pills. *Journal of Financial Economics*, 35(3), 371-390.
- Brickley, J. A., Lease, R. C., & Smith, C.W. (1988). Ownership structure and voting on ant takeover amendments, *Journal of Financial Economics* 20, 267-291.
- Carney, M., & Gedajlovic, E. (2002). The coupling of ownership and control and the allocation of financial resources: Evidence from Hong Kong. *Journal of Management Studies*, 39(1): 123-146.
- Carpenter, M. A., & Westphal, J. D. (2001). The strategic context of external network ties: examining the impact of director appointments on board involvement in strategic decision making. *Academy of Management Journal*, 4(4), 639-660.
- Chami, R. (1999). *What's different about family business?* Working Paper, University of Notre Dame.
- Chang, S. J. (2003). Ownership structure, expropriation, and performance of group affiliated companies in Korea. *Academy of Management Journal* , 46,(2): 238-253.
- Che-Haat, M. H., Mahenthiran, S., Abdul Rahman, R. & Nadiah A. H. (2006). *Journal of Contemporary Accounting & Economics* ,Vol. 2, No I, pp. 99-121.
- Che-Haat, Abdul Rahman & Mahenthiran, S. (2008). Corporate governance, transparency and performance of Malaysian companies, *Managerial Auditing Journal*, 23 (8), 744-778.
- Chee, H. K., & Fauziah, Md Taib (2005, December). *Management ownership and firm performance: Evidence from Malaysia*. Paper presented at the 6th Asian Academy of Management Conference, Ipoh, Perak.
- Chen, C.J.P., & Jaggi, B. L. (2000). The association between independent non-executive directors, family control and financial disclosure. *Journal of Accounting and Public Policy*, 19(4&5), 285-310.
- Chen, Z., Cheung, Y. L., Stouraitis, A. & Wong, A.W.S. (2005). Ownership concentration, firm performance, and dividend policy in Hong Kong, *Pacific-Basin Finance Journal* 13: 43-449
- Chu, W. (2009). The influence of family ownership on SME performance: Evidence from public firms in Taiwan. *Small Business Economic* 33:353-373 DOI 10.1007/s11187-009-9178-6, Accepted: 4 February 2009, published online: 18 March 2009, Springer Science Business Media, LLC. 2009.
- Canyon, M.J. & Peck, S.I. (1998). Board size and corporate governance: Evidence from European countries. *The European Journal of Finance*. 4, 291-304.
- Dahlquist, M. & Robertsson, G. (2001). Direct foreign ownership, institutional investors, and firm characteristics, *Journal of Financial Economics*,5 9, pp.413-440.



- Daraghma, Z. M. A. & Alsinawi, A. (2010). Board of directors, management ownership and capital structure and its effect on performance: The case of Palestine Securities Exchange. *International Journal of Business and Management*. 5 (11), 118 – 127.
- Dalton, D., Daily, C., Johnson, J. & Ellstrand, A. (1999). Number of directors and financial performance: A meta-analysis. *Academy of Management Journal*. 42(6), 674-686.
- DeAngelo, H., & DeAngelo, L. (2000). Controlling stockholders and the disciplinary role of corporate payout policy: a study of the Times Mirror company. *Journal of Financial Economics*, 56(2), 153–207.
- Dehaene, A., Vuyst, V.D. & Ooghe, H. (2001). Corporate performance and board structure in Belgian companies. *Long Range Planning*. 34, 383 – 398.
- Demsetz, H., & Lehn, K. (1985). The structure of corporate ownership: Causes and consequences. *Journal of Political Economy*, 93: 1155–1177.
- Douma, S., George, R. & Kabir, R. (2006). Foreign and domestic ownership, business groups, and firm performance: evidence from a large emerging market. *Strategic Management Journal*, 27(7), 637-657.
- Eisenberg, T., Sundgren, S. & Wells, M.T. (1998). Larger board size and decreasing firm value in small firms. *Journal of Financial Economics*. 48, 35-54.
- Elsayed, K. (2007). Does CEO Duality Really Affect Corporate Performance? *Journal compilation*, Business Administration Department, Faculty of Commerce, Ain Shams University, Main Campus (Western Division), Abbassia 11566, Cairo, Egypt.
- Fama, E. F. (1980). Agency problems and theory of the firm. *Journal of Political Economy*, 88(2), 288-349.
- Fama, E. F. & Jensen, M. C. (1983). Separation of ownership and control. *Journal of Law and Economics* 26, 301–325.
- Fauzias, M. N., Rasidah, M. S., & Hendon, R. (1999). Structure of ownership and corporate financial performance: A Malaysian case. *Malaysian Management Review*, December, 44-48.
- Ferris, S. P., Jagannathan, M., & Pritchard, A. C. (2003). Too busy to mind the business? Monitoring by directors with multiple appointments. *The Journal of Finance*, 53(2), 1087-1111.
- Filatotchev, I. Lien, Y. C., & Piesse, J. (2005). Corporate governance and performance in publicly listed, family-controlled firms: Evidence from Taiwan, *Asia Pacific Journal of Management*, 22: 257–283.
- Ghazali, N. A.M. (2010). Ownership structure, corporate governance and corporate performance in Malaysia. *International Journal of Commerce and Management*. 20 (2), 109-119.
- Gunasekarage, A., Hess, K. & Hu, A. J. (2007). The influence of the degree of state ownership and the ownership concentration on the performance of listed Chinese companies. *Research in International Business and Finance*, 2, 379–395.
- Han, K.C. & Suk, D.Y. (1998). The effect of ownership structure on firm performance: additional evidence. *Review of Financial Economics* 7 (2), 143–155.
- Haniffa, R. M., & Cooke, T. E. (2002). Culture, corporate governance and disclosure in Malaysian corporations. *Abacus*, 38(3), 317-349.
- Haniffa, R. M. & Cooke, T. E. (2005). The impact of culture and governance on corporate social reporting. *Journal of Accounting and Public Policy*, 24, 391–430.
- Haniffa, R. & Hudaib, M. 2006. Corporate governance structure and performance of Malaysian listed companies. *Journal of Business Finance and Accounting*, 33(7-8), 1034-1062.
- Ibrahim, H. & Abdul Samad, F. (2011). Agency costs, corporate governance mechanisms and performance of public listed family firms in Malaysia. *South Africa Journal of Business Management*, 42(3), 17-25.
- Ismail, R. & Abdul Rahman, R. (2011). Institutional Investors and Board of Directors' Monitoring Role on Risk Management Disclosure Level in Malaysia. *The IUP Journal of Corporate Governance*, X(2), 37-61.
- Jackling, B. & Johl, S. (2009). Board structure and firm performance: Evidence from India's top companies. *Corporate Governance: An International Review*, 17(4), 492-509.
- James, H. (1999). Owner as manager, extended horizons and the family firm. *International Journal of the Economics of Business*, 6, (1): 41–56.
- Jensen, M. (1993). The modern industrial revolution, exit and failure of internal control systems. *Journal of Finance*. 48, 831-880.
- Jensen, M. & Meckling, W.H. (1976). The theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics*. 3, 305-360.



- Joh, S. (2003). Corporate governance and firm profitability: Evidence from Korea before the economic crisis. *Journal of Financial Economics*, 68: 287-322.
- Kamardin, H. & Haron, H. (2009). Roles of board of directors: Evidence from Malaysian listed companies. *Corporate Board: Role, Duties & Composition*, 5(1), 22-36.
- Kamardin, H. & Haron, H. (2011a). Board performance and firm performance of Malaysian listed companies. *International Journal of Economics and Accounting*, 2(3), 282-306.
- Kamardin, H. & Haron, H. (2011b). International corporate governance and board performance in monitoring roles: evidence from Malaysia. *Journal of Financial Reporting and Accountin.*, 9(2), 119-140.
- Kets de Vries, M. F. R. (1993). The dynamics of family controlled firm: The good and the bad news. *Organizational Dynamics*, 21(3), 59-71.
- King, M. R. & E. Santor. (2008). Family values: Ownership structure, performance and capital structure of Canadian firms. *Journal of Banking & Finance*, 32: 2423-2432
- Krivogorsky, V. (2006). Ownership, board structure, and performance in continental Europe. *The International Journal of Accounting* 41:176-197.
- Lau, Y. W. and Tong, C. Q. (2008). Are Malaysian government-linked companies (GLCs) creating value? *International Applied Economics and Management Letters*, 1(1), 9-12.
- La Porta, R., Lopez-De-Silanes, F., & Shleifer, A. (1999). Corporate ownership around the world, *Journal of Finance*, 54: 471-514.
- Le, T. V. and Buck, T. (2009). State ownership and listed firm performance: A universally negative governance relationship? *Journal of Management and Government*, 10, 9098-5.
- Lin, S. Y. (Saturday, 3 December, 2011). Corporate Governance Blueprint 2011. The Star Online, available at <http://www.thestar.com.my>
- Lin, C.H. & Shiu C. (2003). Foreign ownership in the Taiwan stock market: an empirical analysis, *Journal of Multinational Financial Manager*, 13, pp.19- 41.
- Lin, Y. C., Huang, S. Y. & Young, S. C. (2008). An empirical study on the relationship between ownership and firm performance: Taiwan evidence, *Afro-Asian Journal of Finance and Accounting*, 1(1), 67-80.
- Makhija, A. K. and M. Spiro (2000) "Ownership Structure as a Determinant of Firm Value: Evidence from Newly Privatized Czech Firms," *The Financial Review*, 41, pp. 1-32.
- Martinez, J.I., Stohr, B.S., & Quiroga, B. F. (2007). Family ownership and firm performance: Evidence from public companies in Chile, *Family Business Review*, 20 (2), 83-94.
- Mat Nor, F. M., Shariff, F. M., & Ibrahim, I. (2002). The effects of concentrated ownership on the performance of firms: Do external shareholdings and board structure matter? *Working paper*.
- Maury, B. (2006). Family ownership and firm performance: Empirical evidence from Western European corporations. *Journal of Corporate Finance*, 12, 321-341.
- McConaughy, D.L., Walker, M.C., Henderson Jr., G.V., Mishra, C.S., 1998. Founding family controlled firms: efficiency and value. *Review of Financial Economics* 7, 1-19.
- McConnell, J. & Servaes, H. (1990). Additional evidence on equity ownership and corporate value, *Journal of Financial Economics*, 27(2), 595-612.
- Minority Shareholder Watchdog Group (MSWG) (2009). *Governance and Transparency Index – Malaysia*. from <http://www.mswg.org.my>
- Mishra, C.S., Randoy, T. & Jensen, J.I. (2001). The effect of Founding Family Influence on Firm Value and Corporate Governance, *Journal of International Financial Management and Accounting*, 12(3),235-259.
- Miwa, Y., & Ramseyer, J. M. (2000). Corporate governance in transitional economies: Lessons from the pre-war Japanese cotton textile industry. *Journal of Legal Studies*, 29, 171-204.
- Mohd Salleh, T., Mohd Iskandar, N. & Rahmat, Mohd-Mohid (2005). Earnings management and board characteristics: Evidence from Malaysia. *Jurnal Pengurusan*, 24, 77-103.
- Morck, R.K., Shleifer, A., & Vishny, R. (1988). Management ownership and market valuation: an empirical analysis. *Journal of Financial Economics*, 20, 293-315.
- Nicholson, G. J. & Kiel, G. C. (2003). Board composition and corporate governance: How the Australian experience informs contrasting theories of corporate governance. *Corporate Governance: An International Review*, 1(3), 189-205.
- Omran, M., Bolbol, A. & Fatheldin, A. (2008). Corporate governance and firm performance in Arab equity markets: Does ownership concentration matter? *International Review of Law and Economics* , 28, 32-45.



- Peng, M. W. (2004). Outside directors and firm performance during institutional transitions. *Strategic Management Journal*, 25(5), 453-471.
- Pfeffer, J. & Salancik, G. (2003). *The external control of organizations: A resources dependence perspective*. Stanford Business Books, Stanford, CA.
- Piesse J., Filatotchev, I., and Lien Y-C (2007). Corporate governance in family-controlled firms in Taiwan. *International Review of Economics*, 54(1), p.176-193
- Perez-Gonzalez, F. (2006). Inherited control and firm performance. *American Economic Review*, 96, 1559-1588.
- Randoy, T., Dibrell, C. & Craig, J. B. (2009). Founding family leadership and industry profitability. *Small Business and Economics*, 32, 397-407.
- Rechner, P., & Dalton, D. (1991). CEO duality and organizational performance: A longitudinal analysis. *Strategic Management Journal*, 12, 155-160.
- Rosenstein, S. & Wyatt, J.G. (1997). Inside directors, board effectiveness, and shareholder wealth. *Journal of Financial Economics*, 44, 229-250.
- Ruhani, A. & Sanda, A.U. (2001). Further evidence on the relationship between board ownership and firm performance in Malaysia. *Capital Market Review*, 9(1&2), 111-124.
- Ruigrok, W., Peck, S. I., & Keller, H. (2006). Board characteristics and involvement in strategic decision making: Evidence from Swiss companies. *Journal of Management Studies*, 43(3), 1201-1226.
- Saito, T. (2008). Family firms and firm performance: Evidence from Japan. *Journal of Japanese and International Economics*, 22, 620-646.
- Sarkar, J. and Sarkar, S. (2009), "Multiple board appointment and firm performance in emerging economies: Evidence from India", *Pacific-Basin Finance Journal*, Vol. 17, pp.271-293.
- Securities Commission. (2007). Malaysian code of corporate governance, <http://www.sc.com.my/sub.asppageid=&menuid=332&newsid=&linkid=&type=s/> (accessed 3 November 2011)
- Securities Commission. (2011). Blueprint on corporate governance, http://www.sc.com.my/eng/html/cg/cg2011/pdf/cg_blueprint2011.pdf (accessed 3 November 2011)
- Shleifer, A., & Vishny, R. (1997). A survey of corporate governance, *The Journal of Finance*, 52(2), 737-783.
- Short, H., & Keasey, K. (1999). Managerial ownership and the performance of firm: evidence from the UK. *Journal of Corporate Finance*, 5(1), 79-101.
- Sraer, D. & Thesmar, D. (2007). Performance and behavior of family firms: Evidence from the French stock market. *Journal of the European Economic Association*, 5(4), 709-751.
- Tan, M. Guo-Sze. (2005, July). *Ownership concentration, board composition and performance in Malaysia*. Paper presented at the 16th AFA Conference, Kuala Lumpur.
- Tan, R. S. K., Chang, P. L., & Tan, T. W. (2001). CEO share ownership and firm value. *Asia Pacific Journal of Management*, 18, 355-371.
- Taylor, R.N. (1975). Age and experience as determinants of managerial information processing and decision making performance. *Academy of Management Journal*, 18(1), 74-81.
- Tian, L., & Estrin, S. (2008). Retained state shareholding in Chinese PLCs: Does government ownership always reduce corporate value? *Journal of Comparative*
- Thomsen, S. & Pedersen, T. (2000). Ownership structure and economic performance in the largest European companies, *Strategic Management Journal*, 21, 689-705.
- Tykvová, T. & Borell, M. (2012). Do private equity owners increase risk of financial distress and bankruptcy? *Journal of Corporate Finance*, 18, pp. 138-150.
- Uadiale, O.M. (2010). The impact of board structure on corporate financial performance in Nigeria. *International Journal of Business and Management*, 5(10), 155-166.
- Villalonga, B., & Amit, R. (2006). How do family ownership, control and management affect firm value? *Journal of Financial Economics*, 80, 385-417.
- Wan Nordin, W. H. (2009). The impact of family-firm structure and board composition on corporate transparency: Evidence based on segment disclosures in Malaysia. *The International Journal of Accounting*, 44, 313-333.
- Wan, D. & Ong, C. H. (2005). Board structure, process and performance: Evidence from public listed companies in Singapore. *Corporate Governance : An International review*, 13(2), 277-290.



- Wei, Z., Xie, F., & Zhang, S. (2005). Ownership structure and firm value in China's privatized firms: 1991-2001. *Journal of Finance and Quantitative Analysis*, 40, 87-108.
- Wiwattanakantang, Y. (2001). Controlling shareholders and corporate value: Evidence from Thailand, *Pacific-Basin Finance Journal*, 9, 323-362.
- Weisbach, M. (1988). Outside directors and CEO turnover. *Journal of Financial Economics*, 20, 432-460.
- Wong, K. A., & Yek, T. C. (1991). Shareholdings of board of directors and corporate performance: Evidence from Singapore. *Pacific Basin Capital Market Research*, 2, 211-225.
- Yammitesri, J. & Herath, S.K. (2009). Board characteristics and corporate value: evidence from Thailand. *Corporate Governance*, 10(3), 279-292.
- Yammitesri, J., & Lodh, S. C. (2004). Is family ownership a pain or gain to firm performance? *Journal of American Academy of Business*, 4(1/2), 263-270.
- Yermack, D. (1996). Higher market valuation of companies with small board of directors. *Journal of Financial Economics*, 40, 185-211.
- Zainal Abidin, Z., Mustafa Kamal, N., & Jusoff, K. (2009). Board Structure and Corporate Performance in Malaysia. *International Journal of Economics and Finance*, Vol.1, No.1, 150-164.
- Zeitun, R. & Tian, G. G. (2007). Does ownership affect a firm's performance and default risk in Jordan? *Corporate Governance*, 7(1), 66-82.



The impact of Corporate Governance on Dividend Payment Policy: empirical evidence from Iranian Listed Companies

Yahya Kamyabi

Department of Accounting, University of Mazandaran, Babolsar, Iran

Seyedeh Zahra Noushabadi

Ayatollah Amoli Branch, Islamic Azad University, Iran.

Abstract

This study aims to examine the relationship between corporate governance and dividend payment policy in listed companies of Tehran Stock Exchange. Hence, we utilized board size, duality of CEO and ownership of institutional shareholders as independent variables and dividend payment policy as dependent variable by controlling firm size, firm growth, financial leverage and return on assets. Using EVIEWS software 7, we applied Ordinary Least Squares (OLS) method to test hypotheses. Based on a sample of 83 listed companies in Tehran Stock Exchange during 2008 to 2012 years, our empirical results indicate that boards size and institutional shareholders are in positive and significant relation to dividend payment policy of the listed companies in Tehran stock, but duality of CEO is not related to dividend payment policy of the listed companies in Tehran stock exchange.

Keywords: corporate governance, dividend payment policy, institutional shareholders, board of director's size, duality of executive manager.

Introduction

For a long time, economists have been long assumed that all related groups to a stock company are operating for a common goal. But there has been proposed various conflicts of interests between groups and how they face with these conflicts by economists over 30 past years. These issues, generally, named as "agency theory in accounting" (Chang et al., 2002). Agency relationship is a



contract on which an employer or owners appoints a representative or agent and delegate to him/her a decision-making authority. In agency relationships, the owners' aim is to maximize their wealth, thus they monitor on representatives' activities and examine their performance to achieve the goal (Arora and Dharwadkar, 2011). Furthermore, corporate governance diminishes agency conflicts between management and shareholders, as improved corporate governance is related to higher earnings quality (Lei et al., 2013). Managers' activities are guided or somehow limited by some factors. These factors should be proposed and deployed more suitably for corporate governance and the companies must observe many rules and regulations by doing their duties and many institutions should monitor on the process of economical units activities. These factors include the items such as board of directors (that have the right to hiring, dismissal and rewarding), rules and regulations, labor contracts, market and even competitive environment. Generally, the above factors can be regarded as two groups of external control mechanisms (such as a market), and internal control mechanisms (such as board of directors) (Karami, 2008).

Monitoring attributable to corporate governance is able to improve the reliability of accounting earnings and improves the effective capability of accounting earnings. Therefore, corporate governance can be used as an effecting factor on earnings reliability. On the other hand, dividend distribution policy is one the substantial subjects of financial literatures in recent years. There has not been yet clearly demonstrated why companies distribute some of their earnings as dividend payment between shareholders and why dividend payment is important for shareholders. So this issue is posed as a puzzle of dividend payment of financial literature. Lei et al. (2013) have stated that dividend payment management cannot results in increasing (decreasing) stakeholders' interest in a complete and effective market. However, capital markets are not completely efficient. According to the rational expectations theory, the shareholders have special expectations about dividend payment from companies (Aharoni, and Javid, 2001). If dividend announcement be corresponded with what the market expects, the prices will not change. But if shareholders recognized the unexpected changes occurred in distributed dividend, they would wonder what the goal of the managers about these changes is. Companies have various policies about dividend distribution, but managers try, regardless of special policies in each company, to distribute dividends in a way that avoid negative changes on shareholders by the help of information about future (Kuan et al., 2011). In this study, we are seeking to examine the relation between corporate governance and dividend payment policy of the listed companies on Tehran stock exchange. There have been done many researches about this field. Hence, Kumar (2003), concluded that there is a relation between ownership structure and dividend payment



policy. Also, Wi and Chang (2003) results demonstrated that there is a nonlinear relationship between dividend distribution policy and ownership structure and state companies tend more to pay cash dividends and public companies prefer to pay higher dividends. Foroughi et al., (2009) results showed that the company's management shares amount have meaningful and positive influence on dividend distribution policy, while institutional shareholders have no influence on dividend distribution policy. Khodadadi & Aghajari (2009) logistic model test results have showed that ownership structure has meaningful influence on dividend distribution policies. According to the obtained evidences from Karami et al., (2010), on the other side, there is a meaningful and positive relationship between institutional concentration and dividend payment which is based on agent theory. Mansourinia et al., (2013) results have demonstrated that there is a considerable and positive relationship between board of director size and dividend payment policy. But the considerable relation between board of director's independence factors and management duality with dividend payment policy has not been seriously regarded. Afzal & Sohrish (2013) believed that board of director's size, individual ownership, firm size and investment opportunities have positive and considerable relationship with dividend amount. On the other hand, internal ownership and profitability of the company have an extremely negative impact on dividend payment. Institutional ownership and leverage have a negative impact, while board of director's independence had positive relationship with payment ratio. Their Logit and Probit models had demonstrated that individual ownership, internal ownership and profitability have negative, positive and considerable relationship with dividends, respectively. Investment opportunities have positive-but insignificant- relationship with dividend-related decisions. Consequently, our hypothesis is as follows:

H1: Board Size is positively associated with dividend payment policy of listed companies in Tehran Stock Exchange.

H2: CEO Duality is positively associated with dividend payment policy of listed companies in Tehran Stock Exchange.

H3: institutional investors are positively associated with dividend payment policy of listed companies in Tehran Stock Exchange.

2- Research methodology



2-1- Research method

The research design of the study is semi-empirical and is done based on post-event approach (via past information). On the other hand, the current study is descriptive-correlational research. This investigation is a kind of quantitative research based on data natures and is regarded as practical research based on the goals. And in order to examine the research hypothesis and given nature of information, the research data is based on past quantitative and real information.

3-2- Research statistical population and samples

The statistical population of the study is the listed companies on Tehran stock exchange during 2008 to 2012. In order to selecting the sample, the companies were selected which limited to the three following conditions:

They have been listed on Tehran stock exchange before 2008. (1)

Their fiscal year should be the Esfand 29th. (2)

Their data should be available. (3)

They must not be or part of investment companies, leasing, banks, insurance and etc. (4)

On the other hand, Cochran is a common formula for estimating sample volume:

$$n = \frac{Nz^2pq}{Nd^2 + z^2pq}$$

In the above formula, usually, the MAXIMUM PERMISSIBLE ERROR (d) is equivalent with 0.05, confidence coefficient 0.95, t=1.96 and the amounts of p & q are 0.5, and population volume is regarded as N. P value is regarded 0.5, because if p=0.5, n would find its possible maximum value and it may cause the sample to be large enough. According to this formula, the population number is 83 in this study.

2-4- The method of data collection

In this study, financial information has been provided of financial statement and explanatory related companies under investigation and to assistance of CDs regarding Tehran stock exchange, the organization of stock website and Tadbirpardaz and Rahavard Novin software.

5-2- Research conceptual model



In this study, the conceptual model is as following:

$$DP_{it} = \alpha_0 + a_1 BRDSIZE_{it} + a_2 CD_{it} + a_3 IO_{it} + a_4 FS_{it} + a_5 ROA_{it} + a_6 FL_{it} + a_7 FG_{it} + \varepsilon_{it}$$

DP_{it} : dividend payment policy

$BRDSIZE_{it}$: board size

CD_{it} : CEO duality

IO_{it} : institutional shareholders ownership

FS_{it} : firm size

ROA_{it} : return on assets

FL_{it} : financial leverage

FG_{it} : firm growth

2-6- Operational definitions of research variables

Table 1-1- Operational definitions of research variables

Variable type	Variable name	Manner of measurement
Independent	<i>Board size</i>	is the board size of firm <i>i</i> in year <i>t</i>
	<i>Duality</i>	is a dummy variable for CEO duality of firm <i>i</i> in year <i>t</i> 1 if CEO is also BOD chairman of the board else 0 is awarded
	Institutional investors	Proportion of large institutional investors owning shares
Dependent	Dividend payment policy	dividend per share average during 1387-1391
control	Firm size	Natural logarithm of total assets
	Return on assets	Net income divided by total assets
	Financial leverage	Total liabilities divided by total assets
	Firm growth	(Current year sales - last year sales) dividend by last year sales



2-7- Data analysis methods

In this paper, combined data are used for testing hypothesis. Time series data (reviewed years) and sectional series data (studied companies) are combined in this method. Combined data are further used to increase observations, enhancing freedom degree, decreasing variance heterogeneity and dynamic study of changes. To estimate the efficiency of a regression model using combined data, common effects, fixed effects or random effects model are selected using suitable tests. One of these tests is F limer test that is used for selecting common effects or fixed effects models. If fixed effects model is selected, Housman test is used for selecting fixed effects and random effects models. So autocorrelation will be examined except disturbance of modal, heterogeneity of variance and normality of data. To determine the explanatory power of descriptive variables (Adjusted R^2), to examine the variables significance and to investigate the overall adequacy of the model, Fisher F statistics are used. Also, statistical analysis is performed by Excel and Eviews software.

3- results

3-1- Descriptive statistics

Table 1-1 description of statistical data

The variable type	The variable name	Minimum	Maximum	Average	SD
Dependent	Dividend payment policy	0.075242	0.42158	0.21659	0.32658
Independent	Size of the board	0.05996	0.62309	0.37458	0.18547
	Institutional shareholders' ownership	3	14	6.59	1.22409
Control	Size of firm	3.6595	26.3059	12.3269	0.6902
	Return on assets	0.15487	0.65985	0.36952	0.05247



	Financial leverage	0.09598	0.51748	0.23605	0.12651
	Firm's growth	0.06552	0.23628	0.11633	0.19962

Pattern	Duality of CEO's duty			
	The number	Percent	Minimum	Maximum
Separating CEO's duty from the chairman of the board or deputy of the board	52	62.73	0	1
Non-Separating CEO's duty from the chairman of the board or deputy of the board				

3-2- Examination of variance heterogeneity

In order to examine the variance heterogeneity, disturbing statements in ARCH-LM test is done in this paper. The results of Arch-LM test variance heterogeneity are as follow table:

Description	Statistics value	Probability
F-statistics	0.748541	0.1050
Obs*R-squared	1.26598	0.1050

As respects to this statistics is not significant at 5% level, so homogeneity of variance is verified and heterogeneity of variance is rejected in disturbing statements.

3-3- F statistics test

Table 3-1- The result of F statistics test

Description	Statistics value	Freedom degree	Probability
Cross-section F	1.226528	82	*0.012



Cross-section Chi-square	142.220696	82	*0.015
--------------------------	------------	----	--------

4-3- Housman test

Table 4-1- The result of Housman test

Description	Statistics value	Freedom degree	Probability
Cross-section F	6.096552	11	*0.021

According to the results of two performed tests (F and Housman), the obtained probability was less than 5% in both tests, so fixed effects method should be used for related regression model.

4-3 Multiple linear regressions

Table 5-1- Regression test for the first hypothesis

Variable	Not-standardized coefficients		T	Sig.
	B	SE		
Fixed	0.322	0.174	2.325	0.002*
Board of director size	0.181	0.311	2.202	*0.000
CEO's duality	0.102	0.255	0.957	0.088
Amount of institutional shareholders' ownership	0.442	0.121	2.001	0.021*
Firm size	0.032	0.185	0.921	0.142
Return on assets	-0.009	0.102	-1.302	0.074
Financial leverage	-0.011	0.209	-2.111	*0.012
Firm growth	0.152	0.242	2.309	0.004*

* 5% error level

Table 6-1- The capacity of determination and significance of whole model



ANOVA		DW	R	
Sig.	F		Adjusted coefficient of determination	Coefficient of determination
** 0.000	6.155	1.779	0.607	0.618

** 1% error level

Regarding the table 5-1, since Camera-Watson statistic test value is determined among 1.5 to 2.5, lack of correlation between errors is not rejected and regression can be used. Due to F value test is significant (6.155) in error level less than 0.01, it can be concluded that research regression model composed of independent, control and dependent variables, is a suitable model and all independent and control variables can determine dividend payment policy. The value of adjusted coefficient of determination is 0.607 and it demonstrates that 60.7% of all dependent variables depend on independent and control variables in this model. Regarding t statistics in 5% confidence level of board of director size, it can be stated that relation of board of director size and amount of institutional shareholders' ownership with dividend payment policy on the listed companies on Tehran stock exchange is significant. Contrary to, there is not a significant relationship between CEO's duality with dividend payment on the listed companies on Tehran stock exchange.

5- Discussion and Conclusion

The study aimed to examine the relationship between corporate governance and dividend payment policy of firms listed on Tehran stock exchange. The results show that the relationship of amount of institutional shareholders' ownership, size of the board and dividend payment policy of firms listed on Tehran stock exchange is significant. These findings are consistent with the findings in Jirapong and Ning (2006), Mithon (2004), Blu (2008), Fakhari and Yousefali (2009), Mansourinia et al. (2013), Kowalski et al. (2007) and Afzal and Souherish (2013). Also the results show that there is no significant relationship between CEO's Duality and dividend payment policy of firms listed on Tehran stock. These findings of the research are consistent with Chidembran and John (1997) and Kumar (2003), Wi and Chung (2003), Harad and Negoun (2006), Jahankhahni and ghorbani (2005), Khodadadi and Aghajari (2009) and Karami et al (2010). Given the research findings, it is recommended that investigators to develop their portfolio take into account corporate governance mechanism (size of the board, CEO' duality and amount of institutional shareholders' ownership) as



well as dividend payment, because opportunistic managers would use distributed dividend as an instrument to cover existence weakness in corporate governance. By detecting this relation, it is necessary that the exchange officials formulate regulations and legal requirements to implement principles of corporate governance companies listed on the stock. Also the existence of labor force market for efficient and active management plays an important role to observe and control the managers, so it seems necessary that such market be made in the country.

References

- Afzal, M., Souherish, S. (2013). Ownership Structure, Board Composition and Dividend Policy in Pakistan, *The Journal of Finance*, 36: 421-463.
- Aharoni, H. and Javid, A. (2001), "The Ownership Structure and Dividend Payout Policy in uk (Evidence from Karachi Stock Exchange 100 Index)", *International Journal of Business Management and Economic Research*, Vol. 1, No. 1, pp. 58-69.
- Arora, P., & Dharwadkar, R. (2011). Corporate Governance and Corporate Social Responsibility (CSR): The Moderating Roles of Attainment Discrepancy and Organization Slack. *Corporate Governance: An International Review*, 19(2), 136-152.
- Blu, C. (2008). "The Determinants of Board Composition: An Agency Theory Perspective", *Managerial and Decision Economics*, Vol. 16, No. 1, pp. 59-69.
- Chung, C. H., and Shiu, C. Y., (2002), "Foreign Ownership in the Taiwan Stock Market - An Empirical Analysis", *Journal of Multinational Financial Management*, 13: 19-41.
- Harad, J. Negoun, L. (2006), "Dividend Policy, Corporate Governance and the Managerial Entrenchment Hypothesis: An Empirical Analysis", *Journal of Business Finance and Accounting*, Vol. 30, No. 9-10, pp. 306-686.
- Fouroghi, Dariush; Saeidi, Ali; Azhdar, Mohsen (1388). "Impact of institutional investors on dividend policy in the listed companies on Tehran stock exchange". *Journal of accounting investigations*, no.2, period 9, p.p: 42-77.
- Jirapong, P., Ning, J. (2006). Dividend Payouts and Corporate Governance Quality: An Empirical Investigation. *Journal of Banking and Finance*, Vol. 95, No. 4, pp. 252-31.
- Karami, Gholamreza; Mehrani, Sasan, Eskandar, Hoda (1389). "Examination of Agency theory and signaling theory in dividend policy: The role of institutional investors". *Journal of accounting developments*, No. 4, period 3, p.p: 142-177.
- Khanchel, M. A., Lozato, L. G., and Rimbey, J. N., (2007), "An Investigation of the Dynamic Association between Agency Theory and Dividend Policy", *Financial Review*, 30: 367-385.
- Khodadadi, Vali; Aghajeri, Valiallah (1388). "Examination of the relation between firm ownership structure and dividend policy in Iran". *Journal of financial accounting*, no.2, period 4, p.p: 106-126.



- Kumar, J., (2003). When financial institutions are large shareholders: The role of macro corporate governance environments. *Journal of Finance*, 61(6), 2975–3007.
- Kowalewski, O., Stetsyuk, I., Talavera, O. (2007). Does Corporate Governance Affect Dividend Policy? *Journal of Financial Economics*, 14: 186-214.
- Kuan, T.-H., Li, C.-S., & Chu, S.-H. (2011). Cash holdings and corporate governance in family-controlled firms. *Journal of Business Research*, 64, 757–764.
- Lei, Q., Lin, B., and Wei, M. (2013). Types of agency cost, corporate governance and liquidity. *J. Account. Public Policy*, 32, 147–172.
- Miton, S, B. (2004), “Dividends and Directors: Do Outsiders Reduce Agency Costs?” *Business and Society Review*, Vol. 110, No. 2, pp. 171–180.
- Mansourinia, Ali; Hassani, Kamran; Sadegh, Neda (1392). "Examination of relation between corporate governance mechanisms and dividend payment policy". *Journal of accounting and auditing investigations*, No. 7, period 4, p.p: 33-52.
- Mehrani, Sasan; Moradi, Mohammad, Eskandar, hoda (1389). "The relation between institutional ownership and conservative accounting". *Journal of financial accounting investigations*, No. 1, period 5, p.p: 47-62.
- Wi, S., Chang, C.H. (2003), “Board Composition, Ownership Structure and Dividend Policies in an Emerging Market: Further Evidence from CASE 50”, *Managerial Finance*, Vol. 34, No. 12, pp. 953-964.



Establish a Balance Scorecard Approach to Enhance Zakat Distribution System in East Coast Region

MUHAMMAD FARIS BIN ZULKIFLI
School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA

fariszul@hotmail.my

ROSHAIZA BINTI TAHA
School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA

roshaiza@umt.edu.my

MOHD RODZI BIN EMBONG
School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA

rodziembong59@gmail.com

Abstract

This paper aims to evaluate the effectiveness and efficiency of Zakat distribution to eight recipients and measure the level of satisfaction of Zakat recipients toward the distribution system by adopting Balance Scorecard (BSC) approach with the additional elements which is Religiosity perspective. In the original BSC approach developed by Kaplan and Norton (1992) there are only for elements of BSC which are Financial, Customer, Internal Business Process and Learning and Growth Perspective. For this purpose mixed method which is combination of qualitative and quantitative approaches has been utilized. As for qualitative method, open interview was conducted to get more understanding on the problems and issues faced by Zakat Institutions in the distribution system. Based on this interview it is found out that the management of Zakat Institutions believes that there is a need of better evaluation system to enhance the effectiveness and efficiency of Zakat distribution system. While for quantitative method questionnaires were circulated randomly to the respondents. Results show most recipients are not satisfied with the management of Zakat distribution specifically the amount of Zakat receives. This is in line with the data which shows the huge amount of undistributed Zakat every year. Based on the results it is crucial for the Zakat institution to improve the system to gain better public confidence in the institutions. Therefore this study is hope can assists the Zakat management system to improve the institution.

Key Words: Balanced scorecard, Zakat management, religious, Zakat Institutions.

INTRODUCTION

Zakat is the third pillar in Islam and fundamental to Islamic economy. Theoretically it has a wide and deep impact on socio-economic development of a nation (Shariff, Wan Jusoh, Mansor, & Jusoff, 2011). In addition Al-Qardawi (1999) describes Zakat as an act of worship to Allah. Zakat collection needs to be distributed to qualified recipients as prescribed by Allah in the Holy Quran. However, in fiqh perspective, zakat is a payment of wealth for the qualified groups that have been stated in Holy Quran (Abdul Majid, 1992). Muhammad Abdul Aziz (1987) stated that zakat is an important mechanism for social justice as it leads to increased prosperity in this world and also leads to increase of religious merit (thawab) in the hereafter as its payment purifies individuals from sins. Countries can gradually solve the economic problems of its society through zakat system



since history has proved that Zakat is a good and practical way to reduce the gap between the rich and the poor if managed fairly according to the Syariah. The rich will continue to enjoy his wealth, provided part of the wealth is distributed to the poor (Din, Yasin, Salleh, & Ghazalba, 1985). In other words, the poor are not being treated as beggars who beg for mercy of the rich. Muslims that meet the conditions of Zakat payments need to pay Zakat as it is compulsory to all Muslims regardless of Zakat on self (Zakat fitrah) or Zakat on wealth.

In Malaysia, Zakat collection has been increased from year to year (Muhammad Syukri, 2002). For instance, the collection of Zakat in Malaysia in 2007 is RM806, 284,072. However, in 2012, the collection of Zakat becomes RM 1,797,604,876. This shows an increasing in the collection Zakat. Due to this increasing of the collection, it shows that public is more aware on the obligation of paying Zakat. Furthermore, there are some factors that contribute to the increase awareness of paying Zakat. Most of the previous studies proved that the factors influenced zakat on income payment is related with the personality value of the zakat payer. Among of them are Arif, Alwi, & Tahir (2011), Bakar & Ghani (2011), Siska and Siswantoro (2012), and Sapingi, Obid, and Nelson (2013). However, Abu Bakar and Rashid (2010) and Hairunnizam et al. (2005) argues that factors that influence individuals motivation to pay zakat on income was not only personality value but also personal satisfaction influence someone for paying zakat on income. Other factors they get are (1) Altruism, (2) Faith, (3) Self-satisfaction, (4) Organization, (5) Reward. In additions, the government decision on granted the tax rebate on Zakat paid which is stated under Income Tax Act 1967 also the contributing factor to the increasing trend in Zakat collection.

Even though the collection of Zakat is increasing, the question raise on how the effectiveness of the distribution of zakat to recipients, does it increase or no change? As mention in Holy Quran, Zakat collected should all be distributed to eight qualified recipients which are al-fuqara, al-masakin, amil, a convert to tame him, al-Riqab, al-Gharimin, fee-sabilillah and finally ibn sabeel. This statement was supported by Al-Qardawi (2005) which stated that Zakat should be distributed to all eight asnaf if the funds are in abundance and the degree of their needs is similar. Zakat institutions should be continuously increasing Zakat collections and to disburse all Zakat collected in the same year so that Zakat institution can be classified as effective and efficient (Hassan, 2005). However, it is found that there were excess in Zakat collection based on the observation of report from Zakat institution. For example, in 2011 and 2012, the collection of Zakat is RM 1,641,114,095 and RM1,797,604,876 respectively, while the distribution of Zakat is RM1,388,184,633 and RM1,461,764,984 respectively. It is found that the excess of Zakat collection in 2011 is RM252,929,462 while in 2012 is RM335,839,892.

From the finding above regarding of excess in Zakat, it shows that the Zakat is not distributed as the same amount of Zakat collected. Embong, Taha and Mohd Nor (2014) stated that the excess of zakat from any group of the asnaf for the current year shall be transferred to the other groups of asnaf who are also the recipients in the current year; and if still remaining, the excess zakat from the zakat collection in the current year shall be added in the collection of zakat from the following year according to the specified asnaf; and if there still have excess of zakat, it should be stored in a zakat fund surplus.

However, through the observation of the report, there is no clear information regarding this matter whether the excess are being carried forward for next year or be stored as surplus in Zakat institution. It is critical because this may affect the credibility of Zakat institution which responsible to provide such information to public and stakeholders. The public and the stakeholders are left unsure whether their contributions are distributed to the qualified eight asnaf. This leads to the negative perceptions by the recipients and others on the management of Zakat institution.

Furthermore, the other issues pertaining Zakat is poverty problem. Islam introduced Zakat that is very precise and effective to overcome the poverty problem and imbalance between the rich and the poor. The poverty problem in Malaysia can be reduced gradually by looking at the increasing trend of Zakat collection. Even though the collection of Zakat shows an incremental from year to year, however, incidence of poverty among Muslims is still very high. Supposedly by paying and distributing Zakat with effective and efficient, poverty problem can be reduced gradually. In order to overcome poverty problem, the distribution and allocation of Zakat should be done effectively and efficiently. This problem should be addressed by the management of



Zakat institutions. Effectiveness of Zakat collection and distribution of Zakat is highly dependent on the management of Zakat institutions. In additions, aspects of the distribution of zakat is a very important aspect because it shows how the zakat fund can have an impact on society and the country in terms of poverty alleviation and economic development (Mannan, 2003; Wess, 2002; and Hassan & Khan, 2007). Therefore, there is a need of performance measurement tool for Zakat institution to be evaluated based on its performances.

It is suggested that BSC is the most suitable multidimensional performance evaluation to be applies in Zakat institution in order to assist the effectiveness and efficiency of Zakat distribution. The BSC is a strategic planning and management system that is used extensively in business and industry, government, and nonprofit organizations worldwide to align business activities to the vision and strategy of the organization, improve internal and external communications, and monitor organization performance against strategic goals. It was originated by Drs. Robert Kaplan and David Norton in 1992 (Kaplan & Norton, 1992) as a performance measurement framework that added strategic non-financial performance measures to traditional financial metrics to give managers and executives a more 'balanced' view of organizational performance (Paul Harmon, 2009).

In addition, BSC is a perfect tool to ensure that Zakat is being distributed to the qualified eight recipients because BSC is a tool to evaluate performance of management from aspect financial and non-financials. By evaluating Zakat institution performance, it can help enhance and improve Zakat Institutions. Besides, by using BSC, the evaluation on management performance is more likely accurate rather than using other method such as returns on investment (ROI), Earning per Share (EPS), etc. This method only focused on financial measurement and Zakat Institution is non-profit organization, Thus, BSC is complete criteria to establish in Zakat institution which is strategically aligns with management efforts to maximize financial and non-financial output (Kaplan and Norton 1992). There are four perspectives in BSC which are financial, internal business process, customer, learning and growth perspective. In financial perspective, BSC tend to evaluate management performance through its financial aspect. Meanwhile, for internal business measures, BSC more focus on evaluating the process, method or approach in conducting the system or business. For innovation and learning measures, BSC focus on training, or employee development and achievement which are sustainable in business. Lastly, for customer measures, BSC focus on customer satisfaction.

From the discussion we can see that original BSC model does not touch on religiosity aspects. Since Zakat institution is religious institution, introducing the fifth perspectives which is religiosity is a good action to be taken. Religiosity perspective in BSC evaluates the Zakat institution whether the management does follow the Shariah laws and regulation as per stated in Holy Quran and Sunnah as well as reflected individual attitudes and behaviours. It is suitable to be adopted in Zakat institutions because Zakat investigates the role of moral values by individuals towards Zakat compliance. By establishing BSC in Zakat institution, the management performance can be evaluated from time to time. So, the management can enhance and improve their performance in order to maximize the payers and recipients satisfaction. It is hoped that by establishing a BSC Approach in Zakat institutions, the Zakat distribution system can be effectively and efficiently enhanced so that the level of customers' satisfaction can be increased.

Therefore the objective of this study is twofold. First it aims to measure the level of satisfaction of Zakat recipients. Second it propose on the fifth element of BSC to touch on the religiosity aspects. To realize this we conduct a survey to cover the eligible asnaf. In summary the results shows that the recipient are not satisfied with the distribution system. The rest of this paper is organized as follows: Section 2 presents the discussion of Zakat distribution, performance measurement in non-profit organization and BSC by reviewing the relevant literature and Islamic principles. Section 3 explains methods conducted to collect and analysis data, Section 4 provides discussions on descriptive statistics of data based on BSC, and finally, Section 5 presents the conclusion.



LITERATURE REVIEW

1. Zakat Distribution

Allah s.w.t God has clearly explained in the Quran about the distribution of zakat which zakat must be clearly stated in the specific distributed to eight recipients (Hairunnizam et. Al., 2009) as in the words of Allah s.w.t in Surah al-Tawbah, verse 60 which means:

“Indeed, charity, alms are only for the poor, the needy, charity managers, the mu'allaf who persuaded him, for (freed slaves), those who owe, for the cause of Allah and of those who by the way, an ordinance that required Allah.”

(Al-Taubah 9:60)

Based on the interpretation of the text, clearly shows there are eight groups of people are eligible to receive zakat. According to Mahmood Zuhdi (2003), this verse gives a clear explanation of the distribution of zakat compared with the problem of determining the source of charity based on the verse detailing instructions. Eight groups were al-fuqara '(the poor), al-masakin (the poor), amil, a convert to tame him, al-Riqab (slave), al-Gharimin (the person who owns the debt), fee-sabilillah (the cause of God) and finally ibn sabeel (traveler who was traveling) (Hairunnizam et. al., 2009). This definition also being spell out in studies by Marhaini, Ahmad, & Mohamad (2012), Bakar and Ghani (2011), Firdaus and Beik (2012) and the most recent study is by Embong, Taha, & Mohd Nor, 2014. Thus the simple definition are summarize from various paper on the definition of eligible asnaf.

Distribution of Zakat can be classified into three categories: distribution based on need and those who got in this category consists of recipients are needy, poor, slaves, debtors and Ibnu Sabil. The second category is the distribution based on the cultivation and encouragement of religious life and moral and recipients who receive assistance for this category is a convert (Muallaf) and fisabilillah. The third category is based on the distribution of incentives and motivates managers and recipients involved Zakat is Amil (Mujaini Tarimin, 2005).

There is no specified explanation to distribute the Zakat amongst the eight groups and about the portion of the Zakat received by each groups neither in the Qur'an nor in the hadith of the Prophet (Al-Abdin, 2002). However, there is several contradictions regarding on the distribution of Zakat based on the categories of recipients. Al-Shafi'i is of opinion that Zakat should be distributed to all the eight categories if they exist, otherwise to those who are available of them and being supported by some of the Hambalites. However, Malik and Abu Hanifah argued and said it is not necessary to cover all groups.

Shahatah, Shawki Ismail (2000) quoted Abu Ubaid (in al-Amwal) to be said that the Prophet (peace be upon him) initially mentioned only one category to receive Zakat in his hadith: “The Zakat is to be collected from the rich and paid back to the poor”. However, when the Prophet received more money/wealth, he mentioned another category that was “those whose hearts are to be reconciled”. Further, when more and more money received, he added another category that was “those who are in debt”. Following this discussion, Abu Ubaid stressed that the distribution of the Zakat fund is to be left to the discretion of the ruler to manage it.

Al-Qardawi (2005) is of the opinion that the funds of *Zakat* should be distributed to all eight asnaf if the funds are in abundance and the degree of their needs is similar. The share of each one should not necessarily be equal but should be according to their number in society and conditions of need. As most scholars are of the opinion that preference should be given to the poor in distributing the *Zakat* fund rather than covering all the deserving categories, it is found that most countries give a greater percentage of the *Zakat* fund to the genuine poor group of people (Al-Abdin, 2002).

Author	Discussion
Al-Shafi'i and Hambalites	Distributed to all the eight categories if they exist, otherwise to those who are available of them
Malik and Abu Hanifah	It is not necessary to cover all groups



Shahatah, Shawki Ismail (2000)	To be collected from the rich and paid back to the poor. When excess, it is to be paid to those whose hearts are to be reconciled. If there are more excess, it is to be paid to those who are in debt
Al-Qardawi (2005)	Distributed to all eight asnaf if the funds are in abundance and the degree of their needs is similar

TABLE 1: The discussion on definition of Zakat.

2. Measurement performance of Non-profit organizations

Zakat institution is a body that being trusted to manage Zakat collection and distribution fund. Zakat institution is a non-profit organization that entitled to ensure the effectiveness and discipline of Zakat payment. Besides, Zakat institutions also obligate to comply with Shariah law and responsible toward administration and management of Islamic fund and also to achieve a target in Zakat usage by following main scale in one place. Thus, there is a need to know how well Zakat institutions fulfill their role that being trusted on collection and distribuion of Zakat. To cater this objective, this paper tends to examines how non-profit organizations should be measured based on its performance. To accomplish this, this paper reviews the previous studies regarding performance measurement in non-profit organization.

Performance measurement for nonprofit organizations, such as Zakat institutions, should include multiple types of measures: inputs, processes, outputs and outcomes (Keehley & Abercrombie 2008). This is due to the varying level of services and monetary aids provided by the institutions. The existence of multiple stakeholders also makes it necessary to include multiple measures to capture organizational performance adequately.

Previous studies have discussed the important in measurement of the performance in non-profit organization. Among of them are Schuster (1997), Berman and West (1998) which is stated that it is important by managers of nonprofit organizations to measure their performance. Furthermore, it is added by Zahra (1991) and Lu (2006) which is said that performance of nonprofit organization should be measured both in terms of its financial and non-financial performance. From these statements, few approaches to measure the performance of non-profit organization have been introduced. Among of them are total quality managements, activity based costing, outcome-based evaluation, balance scorecard, etc. Table 2 below show the definition of few approaches:

Performance measurement tool	Definition
Balance Scorecard	A strategic management and measuring process, used to help align specific business activities with an organization's strategy and vision that designed to help communicate and measure goals and performance (Kaplan and Norton, 1992)
Total quality managements	An integrated effort designed to improve quality performance at every level of the organization (Crosby, 2000)
Activity based costing	An approach to the costing and monitoring of activities which involves tracing resource consumption and costing final outputs (CIMA Official Terminology, 2005)
Outcome-based evaluation	A systematic approach that determines if a program has achieved the desired results (Amanda, 2010)

TABLE 2: The definition of performance measurement tool.

It is suggested for a multidimensional performance evaluation which is Balance Scorecard (BSC) is most suitable which can contribute to the enhancement and improvement of Zakat distribution compared to other approaches to measure performance of non-profit organization such as Zakat institution. Balance scorecard and why BSC being choose to overcome this problem will be discussed in next topic.



3. Balance scorecard

Following framework established by earlier scholars that organizational performance should include both financial and non-financial indicators. There are few approaches that can be used to measure performances such as extreme risk management, total quality managements, activity based costing, outcome-based evaluation, process and impact evaluation, participatory evaluation, evidence-based practice and other in management that can be used to measure performance. However, the most popular and suitable that is widely used to evaluate management performance level in private and public sector is Balanced Scorecard (BSC). This is because BSC has included both financial and non-financial indicators. Marin (2012) proved that the used of balanced scorecard for managers helps to improve their performance. Furthermore, based on previous studies, lot of scholars have supported that BSC is good approach to evaluate performance. Among of them are Braam & Nijssen, (2004), Michalska (2005), Maris Martinsons, Robert Davison, Dennis Tse (2011). Furthermore, Birchard (1996) suggests that the Balanced Scorecard is believed to be successful because of its ability to define the critical success factors and measures that focus on growth and long term success.

A series of literature has conceptually agreed that service quality is a major element that affects long-term profitability of organizations (Reichheld and Sasser, 1990; Zeithaml et al, 1996; Agus et al, 2000). Reichheld and Sasser (1990) stressed that in order for an organization to survive, it needs to deliver quality services. However, even though Zakat institution is non-profit organization that not derives profit, however, for long term, it is needed to evaluate based on its financial perspective. This is supported by Kaplan and Norton (1992) that said although they are called non-financial performance, in the long term this measure actually drives financial performance.

BSC had been introduced by Kaplan and Norton (1992) as a strategic management and measuring process, used to help align specific business activities with an organization's strategy and vision that designed to help communicate and measure goals and performance. It is been emphasize by Allan Mackay (2004) stated that Balanced Scorecard is a management system that maps an organization's strategic objectives into performance metrics in four perspectives: financial, internal processes, customers, and learning and growth. These perspectives provide relevant feedback as to how well the strategic plan is executing so that adjustments can be made as necessary.

Based on Kaplan and Norton (1992), BSC has four perspectives which are financial, customers, internal processes, learning and growth perspective. Michalska (2005) stated that Balanced Scorecard being the useful tool in supporting management processes as it permits the estimation of a firm through different perspectives (financial, customers, internal processes, learning and growth perspective). These four types' perspective measures:

1. Financial Perspective

In this perspective, the question related is "How Do We Look to Shareholders?". BSC tends to measure management performance through its financial measures. In view of Zakat institution, this perspective is the most important perspective to focus on because it includes measures of operating income, return on capital employed and economic value. . The level of customers' satisfaction are based on the financial performances (Chi and Gursoy, 2009; Shafiee, Hosseinzadeh Lotfi, and Saleh, 2014). The better financial performances of Zakat institution, the level of satisfaction of the customers will be higher.

2. Internal Business Perspective

In this perspective, the question related is "What Must We Excel At?". BSC tend to determine what the organization should excel at (both long-term and short-term). Executives recognize the importance of the internal processes in which the organization must excel in order to achieve its financial and customer objectives in this perspective (Kaplan and Norton, 2000).

3. Learning and Growth Perspective

In this perspective, the question related is "Can We Continue to Improve and Create Value?". Learning and growth can be defined as a framework for measuring employee satisfaction, productivity, and retention in the



basis of the BSC (Laske, 2001). This perspective of the BSC identifies the infrastructure that the organization must construct to generate long-term growth and development (Kaplan and Norton, 2000). In other word, this perspective defines how the people, technology, and organizational environment merge to support strategy of the organization.

4. Customer Perspective

In this perspective, the question related is “How Do Customers See Us?”. In this perspective, by understanding how the customers view performance has become a main aspect of performance measurement. For example, if the customers are not satisfied, eventually, they will find another supplier that meets their requirement. In other word, the key to tackle customer loyalty is by a good internal business process so that a good relationship between customers can be created. However, if the internal business process is poor, the customer will be not satisfied with the organizations.

5. Religiosity Perspective

This perspective is a new proposed perspective in BSC as we believe it is more appropriate to be introduced in Zakat institution. In this perspective, the question related is “How Do Organization comply with Islamic Law and Regulations?”. By introducing the fifth perspectives in organizations such as Zakat institutions, it will be able to observe whether the management does follow the Shariah law and regulations as per stated in al-Quran and Sunnah.

Zakat institutions are non-profit organizations. There are very limited researches on the application of BSC as a measurement system or strategic management tool by public sector or non-profit organizations. Thus, designing a customized BSC model by adding new proposed perspective for religious non-profit organizations to validate BSC usefulness as the strategic management performance evaluation is very much in demand.

METHODOLOGY

This research is concerned on Zakat institution management and also recipient of the Zakat. This research is aiming to evaluate the level of Zakat institution management efficiency and also to evaluate the satisfaction of recipients of the Zakat distribution. So, the respondents were being studied in this research management of Zakat institution and also Zakat’s recipients. The research method for this study is mixed method approach which is combination of qualitative and quantitative approaches. For qualitative approach, open interview were conducted while for quantitative approach, questionnaires were circulated and distributed.

1. Questionnaires

The questionnaires were directly distributed to a total of 30 respondents participated in the survey. The questionnaires were circulated and distributed to the Muslim community around Kuala Terengganu. The questionnaires were taken from previous study (Mohd Asri, 2011) and being modified. The respondents are coming from various groups of people. All the questionnaires are being answered accordingly.

The Cronbach’s Alpha for the questionnaires is 0.898 as show in Table 3 for the questionnaire distributed, suggesting that the items have relatively high internal consistency. This Cronbach’s alpha is tested for whole questionnaire which mean including every perspectives of Balance Scorecard. Cronbach’s alpha is a measure of internal consistency, that is, how closely related a set of items are as a group. It is considered to be a measure of reliability. Gliem & Gliem (2003) stated that Cronbach’s alpha reliability coefficient normally ranges between 0 and 1. However, there is actually no lower limit to the coefficient. The closer Cronbach’s alpha coefficient is to 1.0 the greater the internal consistency of the items in the scale. It is noted that a reliability coefficient of 0.70 or higher is considered “acceptable” most social science research situations. In other word, this indicates that the items which are questionnaires’ data collected are acceptable.

Reliability Statistics

Cronbach's Alpha	N of Items
------------------	------------



Reliability Statistics	
Cronbach's Alpha	N of Items
.898	23

TABLE 3: Reliability Statistics

2. Interview

Open interview was conducted to get more understanding the problems and issue that faced by Zakat Institutions nowadays in distribution system. Open interview was conducted because data that cannot be collected from quantitative method can be obtained from this interview session. This is because there are lot things cannot be explained only referring to the numerical data which in quantitative methods. The interview questions were constructed from several previous studies. The session of interview was recorded in order to control the validity and reliability.

In data collection for interview of Zakat management, a permission letter is sent to Zakat institution in Kuala Terengganu in order to get permission to conduct interview. After the permission being approved, the interview is conducted at their places. If there is no answer, follow-up will be executed. The interview session is recorded for data analysis.

DISCUSSION

The measures developed are able to measure Zakat Institution Performance because the measure consists of various aspects which can be divided into financial measures and non-financial measures. For every perspective have its own processes taken in measuring Zakat institution performances. The process taken for every perspective as shown in Figure 1 below:

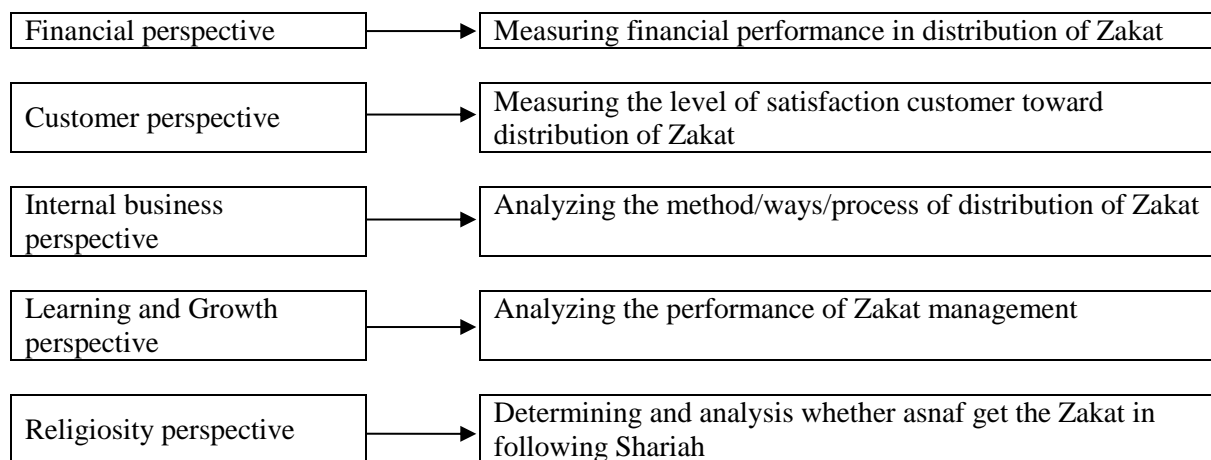


FIGURE 1: The processes taken to measures Zakat institution performances.

1. Financial Perspective

Table 4 below show the descriptive statistics for the financial perspective that being analyzed from questionnaires distributed by using SPSS software.

Descriptive Statistics – Financial Perspective					
	N	Minimum	Maximum	Mean	Std. Deviation
Zakat assistance that were received capable of increasing my monthly income	30	3	5	3.77	.626
Improvement in income that apparent after receiving Zakat assistance	30	2	5	3.90	.803



Zakat assistance that has been given can fill my basic need family	30	2	9	3.90	1.269
The distribution of Zakat is increasing year by year	30	2	9	4.00	1.203
Zakat assistance have made I as a successful businessman	30	2	9	4.03	1.129
All the collected Zakat, being distributed fairly to recipients	30	2	9	4.17	1.315
Zakat assistance can reduce my family poverty level	30	3	43	5.33	7.126
Valid N (listwise)	30				

TABLE 4: Financial perspective

From the descriptive statistics table above, Table 4 shows the variables and mean arrange in ascending order in financial perspective. As we can see, question with the highest mean which is 5.33 is the statement that stated 'Zakat assistance can reduce my family poverty level'. This indicates that most of respondents are agreed with this statement. With Zakat fund receive from Zakat institution through Zakat distribution system, it is found that Zakat fund help in reducing poverty level of a family.

There are two statements that have same mean which is 3.90 is the statement that stated 'Improvement in income that apparent after receiving Zakat assistance' and 'Zakat assistance that has been given can fill my basic need family'. This indicates that the number of respondents agreed and satisfied with this question is same. The lowest mean which is 3.77 is the statement that stated that 'Zakat assistance that were received capable of increasing my monthly income'. This indicates that a few was agreed and satisfied with this question. It is found that from recipients' view, monthly income of recipients does not increase with Zakat fund receive from Zakat institution.

2. Customer Perspective

Table 5 below show the descriptive statistics for the customer perspective that being analyzed from questionnaires distributed by using SPSS software. From the descriptive statistics table above, Table 5 shows the variables and means arrange in ascending order in customer satisfaction perspective. As we can see, question with the highest mean which is 4.13 is the statement that stated 'Zakat assistance already contribute much in improving family education / my children'. This indicates that most of respondents are agreed with this statement. The lowest mean which is 3.80 is the statement that stated that 'Zakat assistance increased my ability in manage Zakat fund that has been given'. This indicates that a few was agreed and satisfied with this question.

Descriptive Statistics – Customer Satisfaction Perspective

	N	Minimum	Maximum	Mean	Std. Deviation
Zakat assistance increased my ability in manage Zakat fund that has been given	30	2	9	3.80	1.349
Zakat contribution increased self potential in improving business potential that is being / performed	30	2	9	3.93	1.230
Zakat assistance already contribute much in improving family education / my children	30	3	9	4.03	1.098



Zakat assistance increased my ability in manage Zakat fund that has been given 30 2 9 4.13 1.196

Valid N (listwise) 30

TABLE 5: Customer satisfaction perspective

3. Internal Business Perspective and Learning and Growth Perspective

Table 6 below show the descriptive statistics for the internal business perspective and learning and growth perspective that being analyzed from questionnaires distributed by using SPSS software.

Descriptive Statistics – Internal Business and Learning and Growth Perspective

	N	Minimum	Maximum	Mean	Std. Deviation
The process to apply Zakat is easy	30	3	9	3.83	1.085
The system that Zakat institution using is good	30	2	9	4.00	1.203
The system of distribution is already good	30	3	9	4.03	1.098
The management of Zakat institution is effective and efficient	30	2	9	4.10	1.155
Overall, Zakat institution performance is effective and efficient	30	2	9	4.13	1.167
The procedure to handle applicants is easy	30	2	9	4.17	1.206
Zakat institution doing a good job in distribution of Zakat	30	2	9	4.17	1.262
There is training for employees and employers	30	3	9	4.27	1.112
Zakat institution gives good services	30	3	9	4.27	1.461
Information regarding Zakat can be obtained easily	30	2	9	4.37	1.129
Valid N (listwise)	30				

TABLE 6: Internal business perspective and learning and growth perspective.

From the descriptive statistics table above, Table 6 shows the variables and mean arrange in ascending order in internal business perspective and learning and growth perspective. As we can see, question with the highest mean which is 4.37 is the statement that stated 'Information regarding Zakat can be obtained easily'. This indicates that most of respondents are agreed with this statement. There are four statements that have two same means which are 4.17 and 4.27. For mean 4.27, the statements that stated is 'There is training for employees and employers' and 'Zakat institution gives good services'. For 4.17, the statements that stated is 'Zakat institution doing a good job in distribution of Zakat' and 'The procedure to handle applicants is easy'. This indicates that the number of respondents agreed and satisfied with this question is same. The lowest mean which is 3.83 is the statement that stated that 'The process to apply Zakat is easy'. This indicates that a few was agreed and satisfied with this question because they felt that to apply the Zakat fund is hard and complicated. There is a lot of procedure taken to process Zakat application.

From the visit in interview session with Zakat institution management at Kuala Terengganu, it is found that there were lot of processes taken to know whether Zakat application is approved or rejected. This statement is



supported by the interviewee of Zakat institution at Kuala Terengganu which is agreed that the process of approval Zakat application is complicated and take long time as show in Table 7.

Interview	In your opinion, how long it will take to process the application of recipient?
Focus group	Actually it depend on recipient’s situation. However, in most cases, there were lot of processes involve to evaluate the recipient’s application and obviously its will take quite a time.
Interview	So, is there any complain regarding this problem? What are recipient’s claim? We do receive lots of complain and we tried to solve every of them. Lots of recipients always complain regarding processes which is complicated and take long time. However, regarding the processes involve, it has been standadized in this state. So, there is nothing much we can do about this matter. All recipient want to recieve Zakat fast, however, we need to evaluate first whether they are eligible or not to recieve the Zakat.

TABLE 7: The conversation occured during interview session.

The flow chart in managing work, overseeing and making recommendations on applications for consideration as recipients of zakat are shown in Figure 2.

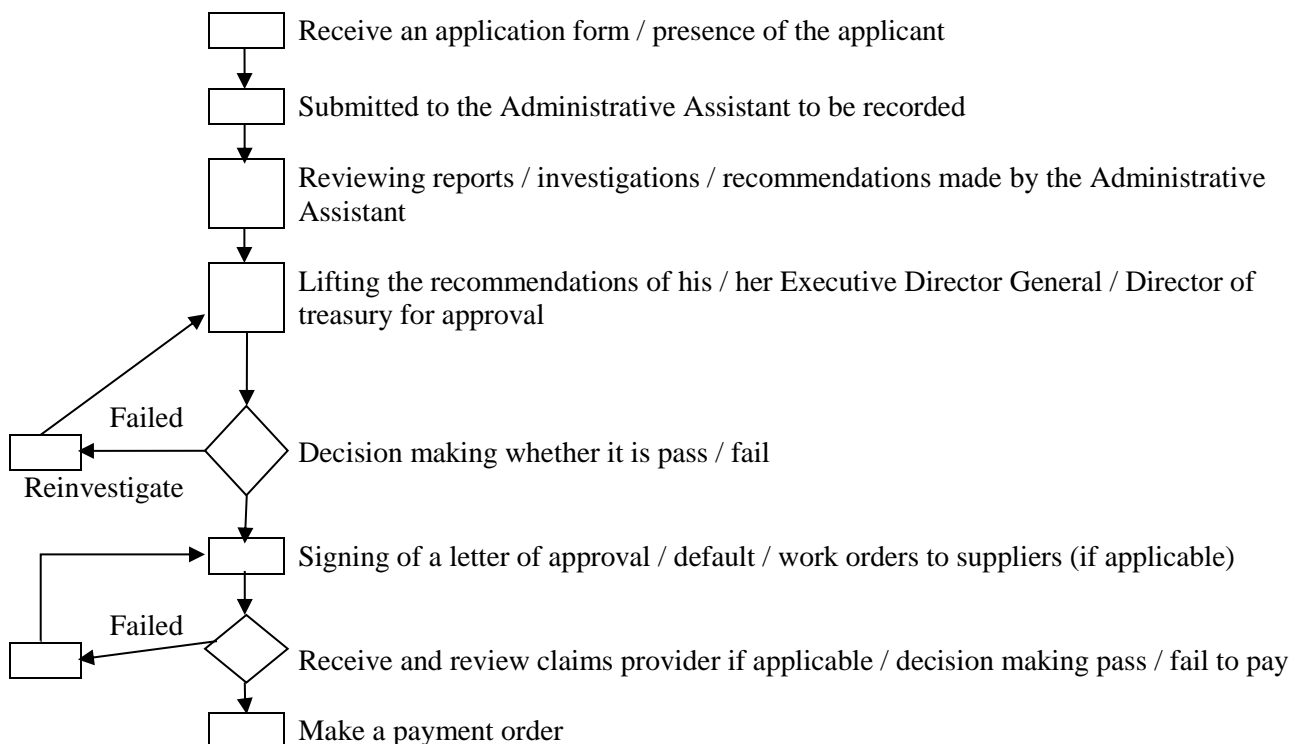


FIGURE 2: The flow chart in managing work, overseeing and making recommendations on applications for consideration as recipients of zakat.

4. Religiosity Perspective

Table 7 below show the descriptive statistics for the religiosity perspective that being analyzed from questionnaires distributed by using SPSS software. From the descriptive statistics table above, Table 8 shows



the variables and mean arrange in ascending order in religiosity perspective. As we can see, question with the highest mean which is 4.70 is the statement that stated 'The institution clearly complied to shariah law'. This indicates that most of respondents are agreed with this statement which is Zakat institutions are compliance to Shariah law. The lowest mean which is 4.47 is the statement that stated that 'The Zakat only been distributed to eight qualified recipients'. This indicates that a few was agreed and satisfied with this question. Some respondents think that Zakat fund are not been distributed to eight qualified recipients.

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
The Zakat only been distributed to eight qualified recipients	30	3	9	4.47	1.106
The institution clearly complied to shariah law	30	3	9	4.70	1.343
Valid N (listwise)	30				

TABLE 8: Religiosity perspective

Based on annual report from 2007 to 2012, it shows that the collection of Zakat increase year by year. However, it is found that the amount of Zakat distribution is not same with amount of Zakat collection. In Shariah law, it said that 'Every Zakat collected must be distributed only to eight qualified asnaf/recipients'. In the annual report, it is reported that there is unallocated Zakat collection and there is no clearly explanation about that matter. It show that Zakat institution does not comply with the statement above. Below is the summary of collection and distribution that being analyzed from annual reports.

CONCLUSION

In conclusion, Malaysia can be considered as one of the outstanding and excellent country in managing Zakat compared to other Islamic countries (Muhammad Syukri, 2002; p. 12). However, the finding shows that, the administration of Zakat in Malaysia is said to be inefficient due to the administration of charity managed by a background of Islamic education but less professional. This causes the distribution of Zakat is not managed properly, effectively and efficiently.

Based on the analysis of descriptive statistics, it is found that the public and the recipients are still not satisfied with the existing Zakat distribution system. In additions, it is found that there is lots of excess in collection of Zakat that not being disclosed or mention in Laporan Zakat based on observation in report. This issue creates negative perception toward Zakat institution. Zakat institutions should have a proper documentation such as in disclosing the excess of Zakat in report which is as one of the responsible toward the public. By doing so, the public and stakeholders can share the information regarding their Zakat contribution. In short, based on these results by evaluating performances using BSC, it can be said that Zakat management need to improve and enhance their performance to cater this issues.

Through this study, the proposed approach is through adoption of multidimensional performance tool by using BSC. It is hoped that by establishing BSC, it might enhance and improve in distribution and also performances of Zakat institution. This is because the management of Zakat institutions is being evaluated to see whether their performance is effective and efficient. If the management is found that not effective and efficient, there is a need a counter measure to improve and enhance the management. In other word, this shows that BSC is a good and suitable tool to evaluate the non-profit organizations, especially in Zakat institutions.

Future research and studies shall focus on the future advantages regard the maintenance and management cost, integration and upgrade as well as scalability issues in the planning phase to avoid waste of money. Another area of future research shall focus or examines to any obstacles that could prevent its implementation.



REFERENCE

- Abdul Majid.M.Z (1992). *Syarat Haul: Satu Penilaian Terhadap Pandangan Al- Qardawi dalam Masalah Zakat Gaji dan Pendapatan Profesional. Medium Vol. 2*, Universiti Malaya
- Abu Bakar, Nur Barizah, & Abdul Rashid (2010). *Motivations of Paying Zakat on Income: Evidence from Malaysia. International Journal of Economics and Finance*, 2 (3), 76-84.
- Al Abdin, Al-Tayib Zein, (2002), 'The Distribution of Zakat', International Training Seminar On Zakah Management, May 20-23, 2002, International Islamic University, Islamabad, Pakistan and Islamic Research and Training Institute (IDB), Pakistan.
- Al-Qaradawi, Yusof. 1999. *Hukum zakat. Singapura: Pustaka Nasional.*
- Al Qardawi, Yusuf, (2005). *A comparative study of Zakat regulations and philosophy in the light of qur'an and sunnah Scientific Publishing Centre, King Abdulaziz University, Jeddah, Kingdom of Saudi Arabia.*
- Arif, H., Alwi, K., & Tahir, A. (2011). Factors influence company towards zakat payment : An explanatory studies, 2nd International Conference on Business and Economics Research (2nd ICBER 2011) Proceeding Factors. (pp. 1-8). Negeri Sembilan.
- Asri, M. A. B. M. (2011). *Keberkesanan pengagihan Zakat terhadap asnaf: Kajian Kumpulan Usahawan asnaf zakat negeri Pulau Pinang.* (Management Faculty report, 2011). Universiti Utara Malaysia.
- Bakar, M., & Ghani, A. (2011). Towards Achieving the Quality of Life in the Management of Zakat Distribution to the Rightful Recipients (The Poor and Needy), *International Journal of Business and Social Science*, 2(4), 237-245.
- Birchard, B., 1996, 'Where Performance Measures Fail', *CFO: The Magazine for Chief Financial Officers*, 12 (10), October, p. 36.
- Braam, G. J. M., & Nijssen, E. J. (2004). Performance effects of using the Balanced Scorecard: a note on the Dutch experience. *Long Range Planning*, 37(4), 335-349. doi:10.1016/j.lrp.2004.04.007.
- Chi, C. G., & Gursoy, D. (2009). Employee Satisfaction, Customer Satisfaction, and Financial Performance: An Empirical Examination. *International Journal of Hospitality Management*, 28(2), 245-253. Doi:10.1016/J.ijhm.2008.08.003.
- Din, H., Yasin, S., Salleh, H., & Ghazalba, S. (1985). *Manusia dan Islam.* Pulau Pinang: Dorong-UBS Sdn Bhd.
- Embong, M. R., Taha, R., & M.N., Nor, M. (2014). Role of Zakat to Eradicate Poverty in Malaysia, *Jurnal Pengurusan* 39(2013), 141-150.
- Firdaus, M., Beik, I. S., & Irawan, T. (2012). Economic Estimation and Determinations of Zakat Potential in Indonesia, *IRTI Working Paper Series (WP# 1433-07)*. Islamic Research and Training Institute.
- F. Schuster. (1997). *Lean thinking; Banish waste and create wealth in your corporation.* Simon & Schuster UK Ltd.
- Gliem, J. A., & Gliem, R. R. (2003). Calculating , Interpreting , and Reporting Cronbach ' s Alpha Reliability Coefficient for Likert-Type Scales, *2003 Midwest Research to Practice Conference in Adult, Continuing, and Community Education*, 82-88.



- Hairunnizam Wahid, Sanep Ahmad & Mohd Ali Mohd Noor (2005), *Kesan Bantuan Zakat Terhadap Kualiti Hidup Asnaf Fakir dan Miskin*. Universiti Kebangsaan Malaysia.
- Hairunnizam Wahid, Sanep Ahmad & Radiah Abdul Kader (2009), "Pengagihan Zakat oleh Institusi Zakat kepada Lapan Asnaf: Kajian di Malaysia," *Kertas Kerja di bentangkan di Seminar Kebangsaan Ekonomi Islam 2009*, APIUM.
- Hassan M.K & Khan J.M. (2007). Zakat, External Debt and Poverty Reduction Strategy in Bangladesh. *Journal Of Economic Cooperation*. 28 (4), 1-38.
- Hassan, N. C. (2007). Sistem Pengurusan Dana Secara Islam: Satu. *Jurnal Pengurusan JWZH, Vol 1. No.2*, pp. 85-101.
- Kaplan, R. S., & Norton, D. P. (1992). *The Balanced Scorecard – Measures that Drive Performance The Balanced Scorecard — Measures*, Harvard Business Review.
- Kaplan, Robert S. and David P. Norton (2001). Transforming the Balanced Scorecard from performance measurement to strategic management, Part I. *Accounting Horizons (March)*. Vol.15, No. 1, 87-105.
- Keehley, P. and Abercrombie, N. (2008) *Benchmarking in the public and non-profit sectors*. San Francisco: Jossey-Bass.
- Laske, O. (2001). *A Learning-And-Growth Metric for Strategy-Focused Organizations* (Pp. 1–23).
- Lu, Y. (2006). IT capability, uncertainty and organizational performance: Development of measures and empirical examination. *Unpublished PhD, The University of Wisconsin*, United States.
- Mahmood Zuhdi Abdul Majid (2003), *Pengurusan Zakat*. Kuala Lumpur: Dewan Bahasa dan Pustaka.
- Mannan M.A. (2003). Public Sector Management of Zakat dalam :*Hannan S.A (eds.). Zakat and Poverty Alleviation. Dhaka: Islamic Economics Research Bureau*.
- Marhaini, W., Ahmad, W., & Mohamad, S. (2012). Classical Jurists' View on the Allocation of Zakat : Is Zakat Investment Allowed ?, *Middle-East Journal of Scientific Research* 12(2), 195–203.
- Michalska, J. (2005). The usage of The Balanced Scorecard for the estimation of the enterprise's effectiveness. *Journal of Materials Processing Technology*, 162-163, 751–758.
- Muhammad Abdul Aziz. 1987. Zakat & Rural Development in Malaysia- An Ethical Analysis of the Concepts of Growth & Redistribution of Income. *Unpublished Thesis*, UM Dissertation Service, Malaysia.
- Muhammad Syukri Salleh, 2002, 'Lokalisasi zakat: satu cadangan teoritis, *Proceedings of Muzakarah Pakar Zakat*. Paper presented at Zakat Specialist Meet, 21-22 December 2002, UKM.
- Nur Barizah, A. B., Abdul Rahim, A. R., & Hafiz Majdi, A. R. (2006). Motivations of Paying Zakat on Income: An Evidence. *Paper presented at the National Seminar in Islamic Banking and Finance 2006: Islamic Wealth Management Prospects, Issues and Challenges*, Kuala Lumpur.
- Paul Harmon (2009). Balanced Scorecard, *Business Process Trends (June)*, Vol 2.
- Sapingi, R., Obid, N., & Nelson, S. (2013). Towards Developing A Disclosure Index for Malaysian Zakat Institutions, *Paper Proceeding of the 5th Islamic Economics System Conference (September)*, 4–5.



Shafiee, M., Hosseinzadeh Lotfi, F., & Saleh, H. (2014). Supply Chain Performance Evaluation With Data Envelopment Analysis And Balanced Scorecard Approach. *Applied Mathematical Modelling*.

Shariff, A., Wan Jusoh, W. N. H., Mansor, N., & Jusoff, K. (2011). A Robust Zakah System : Towards a Progressive Socio-Economic Development in Malaysia. *Middle-East Journal of Scientific Research*, 7(4), 550–554.

Shahatah, Shawki Ismail, (2000 second edition), '*Limitations on the Use of Zakah Funds in Financing the Socio-Economic Infrastructure of Society*', *Management of Zakah in Modern Muslim Society*, seminar proceeding, Islamic Research and Training Institute, Islamic Development Bank, Jeddah, Saudi Arabia, p 57.

Siska, H., & Siswantoro, D. (2012). Analysis of Zakat on income payers' preference in Indonesia (Potency of double Zakat), *3rd International Conference on Business and Economic Research (March)*, 2882-2890.

W. Berman. J. West, (1998). "Responsible Risk-Taking," *Public Administration Review*, vol.58, no.4 (July-August), pp.346-352.

Wess. H. (2002). Reorganizing Social Welfare among Muslims: Islamic Voluntarism and Other Forms of Communal Support in Northern Ghana. *Journal of Religion in Africa*. 32(1).

Zahra, S.A. (1991). Predictors and financial outcomes of corporate entrepreneurship: An explorative study. *Journal of Business Venturing*, 6, 259-285.

School of Maritime Business and Management
Universiti Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA



Corporate Governance and Firm Value: Evidence from Iranian Listed Companies

Seyedeh Zahra Noushabadi

Ayatollah Amoli Branch, Islamic Azad University, Iran

Yahya Kamyabi

Department of Accounting, University of Mazandaran, Babolsar, Iran

Abstract

This study aims to investigate the relationship between corporate governance and firm value of Iranian listed companies on Tehran stock exchange. We selected 81 listed companies on Tehran Stock Exchange during 2008 to 2012. We utilised percentage of active non-executive managers in the board, managerial ownership, institutional ownership, state ownership, ownership concentration, duality of CEO and chairman the board as independent variables and firm value as dependent variable. Ordinary Least Squares (OLS) regression was applied to examine each our hypothesis. According to the research results, we could not find any significant relationship between percentage of active non-executive managers in the board, managerial ownership, state ownership and firm value, but institutional ownership, the duality of duty of CEO are positively associated with a firm value.

Keywords: corporate governance, ownership structure, corporate governance mechanism and firm value.

1. Introduction

In recent years, the concept of corporate governance has become as essential and dynamic aspect of business and attention to it is increasing in today's economy progressively, meanwhile, various improvements have been made on how corporate governance imposes on the global level. As, the international organizations such as Organization for Economic Co-operation and Development (OECD) have provided acceptable international standards (Lin, 2010). This result has been used for



higher education in universities of U.S and Britain; as a result, also the organizations continue to improve their corporate governance systems and there has been made a special attention to shareholders and their relationships, the amount and level of accountability, improving performance of the chairman of the board, auditors and accounting systems and internal control, as well as they are always seeking ways to suitably control and run the organizations (Mahdavi & Miri., 2005). As well, retail investors, institutional investors, accountants, auditors and other factors of money and capital market are informed about the philosophy and needed correction and permanent improvement of corporate governance. Regarding recent financial crisis in U.S and Europe, although this issue has provided a challenge for this conception and its implementation process, it is hope that the problems can be decreased by reviewing the concepts and dimensions of them (Sanjae et al., 2008).

Institutional investors are the main players of the financial markets. Since their penetration has been increased in corporate governance due to accepted privatization policies by different countries, it can be concluded that the institutional investors are important in various corporate governance systems (Ghalibaf Asl & Dargah, 2005). In this regard, Pound (2005) demonstrated that the institutional investors may both negatively and positively influence on firm value. Hence, Wi et al., (2009) had showed that there is a negative and significant relationship between institutional investors and firm value. In contrast, Mingues et al., (2007) believe that it should not be a systematic relation between ownership structure and firm value. Separating executive director's duties from CEO duties causes to clear the accountability scope and eliminate ambiguities in these two parts in one side, moreover, the independent executive director can have effective influence on corporate governance and regarding the interests of all shareholders and stakeholders. According to the Chang & San (2008) view, the duality of duty of CEO can potentially increase being the ultimate decision-makers risk of CEO in the field of financial reporting which finally causes the cost of management behavior (firm value) to be increased. Molodi (2009) demonstrated that there is no significant relationship between percentage of institutional investors' ownership and separating executive director's responsibilities from CEO or CEO's deputy with created value for shareholders.

Since there are other factors that can influence on value level of business unit, it is necessary to regard these factors and their effects. So, Mohammadi et al., (2009) findings demonstrated that there is no significant relationship between ownership structure and firms value. On the other side, according to Chan & San (2008) view, the duality of duty of executive director can potentially increase being the ultimate decision-makers risk of CEO in the field of financial reporting which causes the cost of



management behavior (firm value) to be increased. The findings show that after controlling company's life factors and financial leverage, there is a positive and significant relationship between corporate governance levels with firm value (Banerji et al., 2009). The other findings demonstrate that there is a negative and significant relation between the duality of duty of CEO as a corporate governance factor and firm value (Mat Nour & Solang, 2010). Generally, our main purpose is to examine the relationship between corporate governance and value of the listed companies on Tehran stock exchange. It seems that there has not been performed any researches in our country yet and this study is regarded as a first one in this field.

2- Research methodology

2-1- Research method

This investigation is a semi-empirical one and by means of post-event approach (through previous information). On the other side, present study is a descriptive-correlated research. This is a quantitative research, in terms of the nature of data. According to purposes, it is considered an applicable one. To examine research hypotheses and given the nature of information, research data is based on previous real and quantitative information. In this research, to examine hypotheses, the combined data is being gone to use. In the method, time series data (the years under investigation) is combined to cross-sectional data (the companies under study). The combined data is used further due to increase in the number of observation, raising the freedom degree, reduction in heterogeneity of variance and dynamical study of changes. To estimate a regression model efficaciously using combined data, it will be selected one of the common-effect, fixed-effect, and random-effect models using appropriate tests. In order to select one of the above modals, the F-limer test is used to select common-effect and fixed-effect medals, Housman test will be used to select fixed-effect and random-effect modals if fixed-effect modal is selected. So auto-correlation will be examined except disturbance of modal, heterogeneity of variance and normality of data. To illustrate power of explanation, the explanatory variables of Adjusted R^2 coefficient will be used, to examine significance of variables and total modal's sufficiency, F-statistics will be used. Also, statistical analysis will be complemented by EXCEL and EVIEWS software.

2-2- Research hypotheses

There is a significant relationship between percentage of active non-executive managers in the board and firm value. •



- There is a significant relationship between managerial ownership and firm value.
- There is a significant relationship between institutional investors and firm value.
- There is a significant relation between state investors and firm value.
- There is a significant relation between ownership concentration and firm value.
- There is significant relationship between CEO duality and the chairman of the board and firm value.

2-3- Research statistical population and sample

The research statistical population is the listed companies on Tehran stock exchange. The statistical sample includes the listed companies on Tehran stock exchange that have the following terms:

1. The companies that have been listed before 2008 on Tehran stock exchange.
2. The companies that have been presented on Tehran stock exchange during 2008 to 2012.
3. The companies that their end of financial year was Esfand 29th.
4. The companies that have not change of financial year.
5. The companies that their demand data are available.
6. The companies that are not part of the banks and financial institutions (investment companies, financial intermediation, holding companies, banks and leasing companies).

Time domain of the study is ranged from 2008 to 2012. So the number of sample companies reaches to 81.

2-4- Method of collecting data

In this study, financial information has been provided of financial statement and explanatory related companies under investigation and to assistance of CDs regarding Tehran stock exchange, the organization of stock website and Tadbirpardaz and Rahavard novin software.

2-5- Research model

The following regression model is used in the study:



$$\begin{aligned}
 QTubin = & a_0 + \alpha_1 (\text{Government ownership}) + \alpha_2 (\text{Institutional ownership}) \\
 & + \alpha_3 (\text{Management ownership}) + \alpha_4 (\text{Out directors}) \\
 & + \alpha_5 (\text{Concentration}) + \alpha_6 (\text{Duality}) + \alpha_7 (\text{LnTA}) + \alpha_8 (\text{Leverage}) \\
 & + \alpha_9 (\text{ROA}) + \varepsilon
 \end{aligned}$$

Q-Tubin: company value

Out directors: percentage of active non-executive managers of the board

Management ownership: managerial ownership

Institutional ownership: institutional investors

Government ownership: governmental investors

Concentration: ownership concentration

Duality: duality of CEO and executive director

LnTA: natural log of total assets

Leverage: financial leverage

ROA: return on assets

2-6- Measuring research variables

Table 1-1- Operational definition of the research variables

Dependent variable	Firm value	Tobin Q ratio
	Percentage of active non-executive managers in the board	Active managers who don't have executive responsibility in a company, i.e. the number of these managers are divided by total CEOs and finally, the percentage of active non-executive managers in board of directors is obtained.
	Managerial ownership	Percentage of management ownership (members of board of directors) from shares of the company (i.e. the percentage of all shares of the company which are available to unit management till the end of the special



Independent variable		year).
	Institutional ownership	The owners such as institutions, organizations and etc. that have high capacity to running and governing the corporate (i.e. the percentage of all shares of the company which are available to institutional owners till the end of the special year).
	Governmental ownership	The percentage of shares available to companies and government organizations.
	Ownership concentration	The percentage of shares available to major shareholders (not minority shareholders)
	CEO duality and chief executive	I.e. CEO and executive director doesn't be one person and two different people are responsible for it and it is defined as dummy variable. It means that if this duality exists, it takes 1, otherwise 0.
Control variable	Total assets	Natural logarithm of total assets
	Financial leverage	It is equal with dividing company's total debt in the end of financial period by company's total assets in the end of financial period.
	Return on assets	It is equal with net profit for t fiscal year dividend by ROA in the end of financial period.

3- Results

3-1- Descriptive statistics of the research variables

Table 1-2- Central and distribution indexes of each research variables

Pattern	Number	Minimum	Maximum	Average	SD
Firm value	81	0.0272	2.9858	1.1855	0.70362
State ownership	81	0.06785	0.62325	0.24059	0.05632
Institutional ownership	81	0.5895	0.32569	0.18952	0.02201



Managerial ownership	81	0.06859	0.14255	0.10205	0.03251
Non-executive members of board of directors	81	0.15231	0.62532	0.28754	0.11751
Ownership concentration	81	0.11425	0.82451	0.38952	0.14471
Total assets	81	84918	80122248	3726135	1.03822
Financial leverage	81	0.029	0.755	0.314	0.16912
ROA	81	0.15215	0.63754	0.32325	0.01253

Table 1-3- Descriptive statistics of the research variable

Pattern	Duality of CEO responsibility			
	Number	Percentage	Minimum	Maximum
Separating executive manager's responsibility from deputy of board of directors' responsibility	52	62.73	0	1
Lack of separating executive manager's responsibility from deputy of board of directors' responsibility	29	37.42		

3-2- Examination of Variance heterogeneity

To examine the possible variance heterogeneity, disturbing statements of LM Arch test is used in this study. Then, the obtained results are presented in the below table:

Table 4-1- The results of LM Arch variance anisotropy of research model

Description	Amount of statistics	Probability
F-statistics	0.775214	0.3773
Obs*R-squared	0.622148	0.3773



Since the test statistics are not significant at 5% level, assumption of variance homogeneity is verified and variance heterogeneity of disturbing statements is rejected.

3-3- Significance test of fixed-effect methods

3-3-1- F statistics test

Description	Statistics amount	Freedom degree	Probability
Cross-section F	2.712259	80	0.000
Cross-section Chi-square	119.203391	80	0.000

3-3-2- Housman test

Table 6-1- Housman test results

Description	Statistics amount	Freedom degree	Probability
Cross-section F	16.011547	13	0.0011

According to the results of two performed tests (F & Housman), the obtained probability was less than 5% in both tests; hence, fixed-effect method must be used in related regression model.

5-3- Multiple linear regression

Table 8-1- Regression results- Rating the quality of financial information disclosure

Variable	No standardized coefficients		T	Sig.
	B	SE		
Fixed	0.325	0.199	2.448	*0.001
State ownership	-0.258	0.058	-1.447	0.068



Institutional ownership	0.309	0.187	2.011	*0.005
Managerial ownership	0.047	0.288	0.966	0.102
Non-executive members of board of directors	0.016	0.166	0.755	0.224
Ownership concentration	0.187	0.072	1.965	*0.017
Duality of executive manager responsibility	0.042	0.344	2.116	*0.006
Total assets	0.075	0.205	1.247	0.081
Financial leverage	-0.247	0.182	-0.672	0.266
Return on assets	0.005	0.168	2.247	*0.002

* 5% error level

Table 9-1- Significance of all models

ANOVA		DW	R	
Sig.	F		Adjusted coefficient of determination	Coefficient of determination
** 0.000	6.299	2.321	0.482	0.488

* 1% error level

According to 8-1, regarding to the significant level of T-test in 5% error level less, it can be concluded that relationship of institutional ownership, concentration ownership and duality of executive director's duty with firm's value is significant. And contrary to, relationship of governmental ownership, managerial ownership and non-executed members in the board with firm's value is not significant. On the other side, due to value of Watson-Camera statistics in range of 1.5 to 2.5, the hypothesis of non-correlated errors is not rejected, and the regression can be used. Considering significance of F-test value (6.299) in error level less than 0.001, it can be that regression model of the



research combined by independent, control and dependent variables is a suitable model, and independent variable is enabled to determine the changes occurring in firm value. The value of adjusted coefficient of determination (R^2) which is equal with 0.482 shows that 48.2% of all firm value changes depends on mentioned independent and control variables in this equation.

4- Discussion and Conclusions

The study aimed to examine the relationship between corporate governance and firms' listed on Tehran stock exchange. The results show that the relationship of institutional ownership, concentration ownership and duality of executive director's duty with firm's value is significant. These findings are consistent with the findings in Nor and Sulong (2010), Smith et al. (2011), Abbasi et al. (2012) and Moushki et al (2009). Also the results show that the relationship of governmental ownership, managerial ownership and non-executive members in the board with firm's value is not significant. These findings of the research are not consistent with Lella and Silva (2005) and Silvira (2007), Mat Nor and Sulong (2010), Chang and Sun (2008) and Moushki et al. (2009). Given the research findings, it is recommended that to expanding the companies' activities range and needing to experts managers to improving accountability policy and enhancing information transparency in companies and economic units that some or all of their capitals are provided by shareholders, it is better for executive director of company to use separated members of the board in order to eliminate all ambiguities in both duties for corporate governance. It is recommended also that to better use of obtained results and help to illustrate influence of CEO duality on firm value, this study should be repeated after adopting and enforcing the corporate governance regulation of the listed companies on Tehran stock exchange.

References

- Banerjee, A., Gokarn, S., and Pattanayak, M. (2009). Corporate Governance and Market Value:Preliminary Evidence from Indian Companies. Standard and Poor's Financial Services LLC.12(2): 42-77.
- Chang, J., and Sun, C. (2008). The Relation between Earning Information, Earnings Management and Corporate Governance in the Pre – and post – Sox Periods. Journal of Accounting and Management, 15(3): 35-48.
- Ghaybaph, H. Ranjbar dargah, F. (2005). Evaluating impact of ownership type on firms' performance (the experiences for privatization in Iran). Journal of financial researches, 19: 117-133.
- Gaa, J. (2007). Corporate Governance, Transparency and Secrecy:The Ethics of Earnings Management. Working Paper: University of Alberta.



- Lin, F. (2010). A Panel Threshold Model of Institutional Ownership and Firm Value in Taiwan International Research, *Journal of Finance and Economics*, 42: 1450-2887.
- Minguez-Vera, A. & Martin-Ugedo, J.F. (2007). Does ownership structure affect value? A panel data analysis for the Spanish market. *International Review of Financial Analysis*, (16): 81-98.
- Mahdi, A., Medri, A. (2005). The structure of ownership and active companies' efficiency on Tehran stock exchange, *Journal of Economic Researches*. 172: 103-132.
- Moloudi, A. (2009). The relationship between corporate governance and shareholders established value. M.S thesis, Economic sciences faculty of Tehran.
- Mouhammadi, Sh., Ghalibaph asl, H., and Moushki, M. (2009). Evaluating impact of ownership structure (combination and concentration) on return on companies' value listed on Tehran stock exchange. *Journal of financial researches*, 15: 15-32.
- Mat nor, F, Sulong, Z. (2010). Corporate Governance Mechanisms and Firm Valuation in Malaysian Listed Firms. *Journal of Modern Accounting and Auditing*, 6(1): 18-36.
- Priya, P.V. & Shanmughan, R. (2011). Foreign Ownership Structure and Corporate Performance: Empirical Evidence from India, *Global Journal of Finance and Management* 3(1), 15-24
- Pound, J. (2005). Proxy contests and the efficiency of shareholder oversight, *Journal of Financial Economics*, 20: 237-65.
- Schmid, M. M., Oesch, D., and Ammann, M. (2011). Corporate Governance and Firm Value: International Evidence. *Journal of Empirical Finance*, 18(9): 75-99.
- Wei, Z. & Xie, F. & Zhang, S. (2009). Ownership Structure and Firm Value in Chinas Privatized Firms, *Journal of Financial and Quantitative Analysis*, 40 (1): 87-105.



Financial literacy and communication of financial ratios

NORHANI ARIPIN
 NOOR AFZA AMRAN
 School of Accountancy
 College of Business
 Universiti Utara Malaysia
 06010 UUM Sintok, Kedah
 MALAYSIA
 norhani@uum.edu.my, afza@uum.edu.my

Abstract

Prime Minister of Malaysia has launched the Economic Transformation Programme (ETP) on 25 October 2010 with aims to transform Malaysia into a high-income nation by 2020. One of the focus of ETP is to boost the National Key Economic Areas (NKEAs). There are twelve NKEAs specified for ETP, and one of them is Financial Services. It is claimed that generally low level of financial literacy among Malaysian public is a challenge for the Financial Services sector. As financial information is not only useful for business community, several regulatory bodies have taken initiatives to enhance the financial literacy not only for investors, but also for the public.

In responding to financial illiterate challenge, this research is conducted to investigate initiative taken by companies to enhance the understandability of investors/ potential investors about firm financial performance. Specifically, this study is looking at the communication of financial ratios in the companies' annual reports for 2011 by top 100 listed companies on Bursa Malaysia. A set of financial ratios is chosen because of the popularity of this technique as financial analysis tool, its simplicity, yet voluntary nature of disclosure in the official annual reports.

Descriptive result reveals on average, 18.4% of the selected ratios were disclosed in the annual reports. The most popular ratios are net assets per share, return on equity, return on assets and gearing. It is suggested that further research may include more number of companies listed on Bursa Malaysia and integrate longer period of study. Government-linked and family companies; as well as small medium enterprises (SME) also could provide further insight. Using survey and interview techniques potentially contribute further about this unique financial reporting practice.

Key Words: Financial ratios, financial literacy, disclosure

INTRODUCTION

Prime Minister of Malaysia has launched the Economic Transformation Programme (ETP) on 25 October 2010 with aims to transform Malaysia into a high-income nation by 2020. In addition, this programme is also targeting Malaysia to become an advanced, developed nation with an economy possessing the characteristics that are common to developed nations (ETP, 2010).

The ETP focuses on key growth engines or National Key Economic Areas (NKEAs). NKEA is defined as a driver of economic activity that has the potential to directly and materially contribute a quantifiable amount of economic growth to the Malaysia economy. There are 12 NKEAs that are the Oil, Gas and Energy; Palm Oil; Financial Services; Tourism; Business Services; Electronics and Electrical; Wholesale and Retail; Education; Healthcare; Communications Contents and Infrastructure; Agriculture; and Greater Kuala Lumpur/ Klang Valley. Overall, these NKEA sectors are sectors in which Malaysia has current or potential competitive



advantage, representing a mix of service, manufacturing, agriculture and extractive industries. These sectors are spread across urban and rural areas and are likely to support growth in the rest of economy (ETP, 2010).

One of the critical NKEAs is the financial services. There are several challenges ahead in this sector as stated in Chapter 7 of the ETP including the low levels of financial literacy. It is suggested that the level of personal financial literacy today is low overall. With growing consumerism as well as changing customer expectations, there is a need to reinforce greater financial literacy to help the Rakyat to better manage their personal finances in line with our move to a high-income economy. Proper consumer education is needed if growth engines, such as private pensions, wealth management and asset management, with their more complex and sophisticated products, are to take off (ETP, 2010). However, as reported in the recent annual report of ETP, there is a need to improve on the existing low levels of personal financial literacy among the country's population (ETP, 2013). This implies that after 3 years of the implementation of ETP, the level of financial literacy is still a challenge for this financial services sector.

According to Atkinson and Messy (2012), a financially literate person will have some basic knowledge of key financial concepts. In addition, financial literacy initiatives would be a platform to gain necessary knowledge, skills and tool for consumers to make informed financial decision (Ali, 2013). Consequently, consumers will be able to manage their wealth efficiently, protect themselves from any fraud and demand for better services when they have appropriate level of financial knowledge.

Many developed countries such as Australia, New Zealand and Singapore have already implemented national strategies on financial literacy. As for Malaysia, various organizations such as Bank Negara, Securities Commission (SC), the Securities Industry Development Corporation (SIDC), and Bursa Malaysia have launched various initiatives to educate their customers to become more financial literate. For example, Bank Negara supports the financial education initiative at the national level by formulating policies and strategic directions. It includes Financial Sector Master Plan 2001-2010 and Financial Sector Blueprint 2011-2020, integration into school curriculum such as school adoption programme and school financial club; and also adult education via AKPK (Credit Counselling and Debt Management Agency).

Further, SIDC also has various financial literacy programmes as early as kid at schools, teenagers, students at university campuses, and Malaysian investors as a whole. For example, financial literacy can start from a simple view of money management for kids from primary school, including saving money, smart spending habits and how to plan finances at an early age. It also can be knowledge of budgeting and savings, the different between needs and wants and also basic knowledge on investment for secondary school students. At the university level, financial literacy can be a knowledge related to financial planning and investing. The focus is on how university students should manage their money once they earn the money in the future

However, these efforts need to be more focused and better coordinated to increase their effectiveness and reach. This is because Malaysian may not yet sufficiently financially savvy as we have the highest level of household debt to GDP in Asia (about 77%), lack of sufficient knowledge and skills to prepare for retirement and making uninformed investment decision (ETP, 2010).

Scope of the study

The level of financial literacy can varies from various perspectives. For example, it can be different from sophisticated and non-sophisticated users of financial information, public people such as school children, teenagers, universities and colleges' students and adults. The financial information is not only useful for users that directly utilize such information such as investors, but also for a large group of public people. Nowadays,



financial products become more sophisticated and complex, thus consumers in general need sufficient level of financial literacy to help them in making informed and conscious financial choices.

Further, another category group of people that relevant to the financial literacy is investors, which is the focus of this research. To educate Malaysian investors, SIDC is established so they are protected from fraudulent transactions and able to make choices as informed market participants. SIDC educates and alerts the investors on various issues, such as investors' protections, rights and responsibilities. One of the issues raised by SIDC is obligation of companies to disclose information in the annual reports according to Companies Act 1965. It is advised that investors should understand what is important in the annual report. As there are various information provided in the annual reports, investors should be sufficiently financially literate to pick up important information to enable them to make informed decision making.

It is also mandated that directors and accountants of the firm should disclosed information that affects the decision making of the investing public. The directors must give a true and fair view of the company's affair and they must not omit or misstate important information. It takes experience, knowledge and skills for investors to digest and choose relevant information for them. Since there is huge range of information provided in the annual reports, some investors potentially just ignore the documents. Further, SIDC also reminds investors that it is not easy to read annual reports. Judgments should be made based on facts, and not on publicity or propaganda. The important details in the annual reports are sometimes hidden between the lines, and investors are suggested to know how to read between the lines to get accurate information.

In addition to the information provided in the annual reports, investors also can get information from research analysts of stock broking companies and fund management companies. However, extra careful should be exercised when digesting information from these parties because they have their own way to analyze and recast accounting information before produce their own report, as compared to what is provided by the companies in the official annual reports. Sometimes, information provided by these two sources is conflicting and confusing.

There are many initiatives offered by various bodies such as Bank Negara and SIDC in helping community to improve the level of financial literacy. However, the focus of this study is looking at initiatives offered by companies in enhancing investors and potential investors understanding about companies' performance. Specifically, this study is looking at unique information disclosed in companies' annual reports to assist investors in making informed decision making. The special and unique information investigated in this is financial ratios. Thus, the objective of this research is to investigate what financial ratios is communicated by companies in the annual reports to portray the financial condition of companies.

LITERATURE REVIEW

Financial Ratios

For the purpose of this study, a financial ratio is defined as a mathematical relation between two quantities (Subramanyam and Wild, 2009). Financial ratios are among financial statement analysis tool that are widely used in communicating financial performance of the firms. It is a popular tool used by various parties such as companies, financial analysts and brokers to convey the financial performance in a simple way. In order to understand financial ratios, it is assumed that the readers should have basic financial knowledge. To be meaningful, financial ratios should be interpreted correctly by readers.

Financial ratios are being taught in most business degrees worldwide. If students taking any business and finance papers, one of the critical topics covered are financial ratios. Financial ratios are useful in assisting



decision making because of its simplicity, easy, yet powerful tool. It would be meaningful if it comes together with diagrams or graphs and comparison between years or companies and industries.

However, some argued that financial ratios are too simple to convey financial position and can be easily manipulated because of its simplicity. It can be manipulated through the manipulation of its formula. Further, it is challenging to compare between companies because companies could use different formulas for similar ratios. Thus, comparable issues is challenge for this tool, unless if the specific ratios used exactly the same formulas.

The disclosure of financial ratios in the annual report currently is on voluntary basis, except for earning per share. Thus, it is believed that companies which provide financial ratios potentially confident with the benefits of disclosing financial ratios in their annual reports. Financial ratio disclosures are critically important for several reasons. First, the disclosures could serve as the crucial information for users of financial statements, including sophisticated or non sophisticated users. Sophisticated users are reliant on disclosed financial ratios to assess the performance of companies. Therefore, providing a comprehensive set of financial ratios and how each was defined are crucial sources of information. For non-sophisticated users, the financial ratio disclosures will enable them to make an informed investment decision making. In addition, many ratios computed today are not standard. Thus, the financial ratio disclosures are essential to overcome these problems.

Despite their wide use and stated importance, there typically is a paucity of financial ratio information disclosed in company's annual reports. In recent years, there has been increasing interest in financial ratio disclosures. Gibson (1982) provides a list and description of ratios that are frequently used in annual reports. Watson, Shrives and Marston (2002) investigate the relationship between financial ratio disclosures and firm characteristics in U.K, while Australian companies were studied by Mitchell (2006) on their selectivity of reporting. In Malaysia, Abdullah and Ku Ismail (2008) investigated the association between accounting ratios and performance of the firms. They found low level of disclosure. Ho, Aripin and Tower (2012) analyzed the impact of corporate governance mechanisms and firm characteristics on financial ratios disclosure over the turbulent 2001 and 2006 periods in Malaysia. They found the highest category of financial ratio disclosures are profitability. To date there has been little agreement on what should be disclosed due to the voluntary nature of financial ratio disclosures (with the notable exception of EPS).

In responding to financial illiterate problem facing by financial information users, this research is undertaken to examine the initiatives provided by the Malaysian companies in assisting financial users to understand companies' financial position in a simple way. The communication of financial ratios is measured as pre-defined ratios provided or reported by companies in their annual reports. Thus, this study is focusing on financial reporting made by companies in communicating voluntary, yet important information in their annual reports to facilitate their investors and potential investors in understanding the financial conditions of the firms before making informed business decisions.

Information provided in the annual reports

This section provides insights into the benefits of providing information in the annual reports. It is based on the argument that firms should provide sufficient decision-useful information to their stakeholders. Knauss (1964, p.607) posits that "disclosure, however, is not a simple method of regulation having universal application and universal effectiveness. It assumes a different role and meaning depending on the information to be disclosed, and the parties for whom the information is intended".

Botosan (2006) suggests public disclosure mitigates information asymmetry by displacing private information and concludes that greater disclosure reduces cost of equity capital. Further, Lundholm and Winkle (2006)



develop and utilise the same theoretical framework in summarising the existing empirical work in the voluntary disclosure area.

Diamond and Verrecchia (1991) find that disclosure reduces information asymmetry and cost of capital. Thus, more disclosure benefits both the firm and its stakeholders. In a related study, Healy, Hutton and Palepu (1999) study the relationship between share performance and extent of voluntary disclosure. They report that increased disclosure is associated with increases in stock performance, growth in institutional ownership, increased stock liquidity and higher analyst coverage.

Lang and Lundholm (1996) found that by disclosing more future information, it reduces uncertainty and information asymmetry, improves accuracy of users expectation and it also could attract the attention of analysts. In addition, provision of forward looking information reduces the cost of capital. Thus, it implies that more disclosure of future-orientated information reduces uncertainty of users.

Evans and Sridhar (2002) investigate how disclosure may influence capital markets, product markets and shareholder litigation. They argue that favourable disclosure lead to a lower cost of capital. Graham, Harvey and Rajgopal (2005) list five factors that motivate firms to voluntary disclose information. These are information asymmetry, increased analyst coverage, corporate control test, stock compensation and management talent. On the other hand, they suggest constraints on voluntary disclosure which are litigation risk, proprietary costs, political costs and agency cost, and limitation of mandatory disclosure precedent that may be hard to maintain.

To conclude, previous studies have reported ample evidence on the positive impact of disclosure to the firms and shareholders. Several studies have applied agency theory in explaining the choice of disclosure policy by the firms. It is suggested that voluntary disclosure, in addition to mandatory disclosure, reduces the information asymmetry problem and therefore enhances better informed decision making. This notion applies to voluntary financial ratio disclosures.

METHODOLOGY

Sample Selection and Data Source

The sample companies are selected from top 100 companies listed on Bursa Malaysia for 2011. These high profile companies are selected because the aim of study is looking at the initiatives provided by companies in communicating financial information. It is believed that these high profile companies are pro-active in assisting government to realise the national agenda, ETP. The year 2011 is considered as a one-year period after government's announcement of ETP. The annual reports were gathered and the data were hand collected. A score of 1 is given if the company provides the pre-determine ratios, otherwise 0. The data is analyzed and descriptive result is presented in the next section.

EMPIRICAL RESULTS

Table 1 provides the list of financial ratios investigated in this study, together with their definitions. These items are selected due to their popularity. The companies' annual reports were analysed to see whether the sample firms provide these financial ratios in the annual reports or not. This study limits to ten ratios because these are the most popular ratios reported by companies. Other ratios potentially will have very low disclosure and the percentage is very small.

Financial ratios can be classified into several categories. It can be divided as share market measure, profitability, capital structure, liquidity and cash flow ratios. As shown in Table 1, net assets per share, dividend payout, dividend yield, return on shareholder and price-to-earning are categorised as share market measure



ratios. In addition, return on equity, return on assets and gross profit margin are classified as profitability ratios. While gearing and debt to equity ratios are labelled as capital structure ratios.

TABLE 1: List of ratio and definition

	Financial ratio	Definition
1.	Net Assets per Share (NAPS)	Measure firm's value per share.
2.	Return on equity (ROE)	Measure profit a company generates with the money shareholders have invested.
3.	Return on assets (ROA)	Measure profit of a company relative to its total assets
4.	Gearing (GEA)	Measure the extent to which company's operations are funded by lenders versus shareholders
5.	Dividend payout (DP)	Measure how well earnings support the dividend payments
6.	Dividend yield (DY)	Measure how much a company pays out in dividends each year relative to its share price
7.	Return on shareholder (RS)	Measure a return of a stock to an investor
8.	Price to earnings ratio (PE)	Measure company's current share price compared to its per-share earnings.
9.	Gross profit margin (GPM)	Measure the proportion of money left over from revenues after accounting for the cost of goods sold.
10.	Debt to equity (DE)	Measure the proportion of equity and debt the company is using to finance its assets.

Table 2 illustrates the frequency of selected ratios communicated by the firms in their annual reports. On average, 18.4% of the selected ratios are reported by the sample firms in their annual reports. Based on the table, the net assets per share ratio is among the popular ratios presented in the annual reports, where 73% of the sample firms provided this ratio. This ratio can be classified as share market measure ratio and provides indicator about the firm's value per share. In order to attract investor or potential investors' attention, providing this ratios could be helpful. This is the potential reason why most companies provide this ratio in their annual reports.

The next most commonly presented financial ratio is return on equity (ROE) where 33 firms reported this ratio. This is a profitability ratio, where investors can have clues about how much profit a company generates with the money shareholders have invested. Providing this ratio to investors also potentially would enhance the understanding of investors about firms' performance. Further, return on assets (ROA) was communicated by 19 companies. This ratio provides an indicator of how profitable a company is relative to its total assets. ROA gives an idea as to how efficient the management is at using its assets to generate earnings. Similarly, this ratio indicates the profitability of the firms. As the aim of companies is making profit, showing these profitability ratios in the annual reports might assist companies provide some indicator about how their companies 'performance. In general, higher profitability ratios signal better performing companies.

Another category of ratios reported by the sample firms is gearing. 16% of the firms provide this ratio in their annual report. Gearing is a measure of a company's financial leverage and shows the extent to which its operations are funded by lenders versus shareholders. The appropriate level of gearing for a company depends on its sector, as well as the degree of leverage employed by its peers. This ratio is categorised as capital structure ratios. Shareholders and lenders are interested with this capital structure ratio because this ratio



portrays the proportion of their contributions towards the operations of companies. Companies that communicate this ratio potentially want to indicate whether their companies are mostly funded by lenders or shareholders. There are various arguments that proposed funding by shareholders is better because it's cheaper than lenders.

The next two ratios communicated by the firms are dividend payout and dividend yield, where 14 and 10 firms respectively communicated these ratios. The payout ratio provides an idea of how well earnings support the dividend payments. A stable dividend payout ratio indicates a solid dividend policy by the company's board of directors. These ratios are categorised as share market measures because these ratios are directly related to shareholders. These are financial ratios that companies would like to highlight in their annual reports to indicate about dividend to their shareholders since dividend is among the main interest of shareholders as a return to their contribution. Thus providing these ratios in the annual reports might attract investors and potential investors' attention.

The remaining four ratios (return on shareholders, price to earnings, gross profit margin and debt to equity ratio) are less reported by companies in their annual report, less than 10%. The potential reason probably because companies give less attention to these ratios and focus more on the previously discuss ratios as their main aim.

TABLE 2: Frequency of individual ratio

	N	Percentage
Net assets per share (NAPS)	73	73%
Return on equity (ROE)	33	33%
Return on assets (ROA)	19	19%
Gearing (GEA)	16	16%
Dividend payout (DP)	14	14%
Dividend yield (DY)	10	10%
Return on shareholder (RS)	7	7%
Price to earnings ratio (PE)	6	6%
Gross profit margin (GPM)	5	5%
Debt to equity (DE)	1	1%

CONCLUSION

In summary, annual reports and financial ratios do play a significant role in conveying the financial information to the users in making informed decision. Sometimes, users do not realize that the important details in the annual reports are sometimes hidden between the lines, and users are suggested to know how to read between the lines to get accurate information. This is where the communication of financial ratios in the annual report comes into the picture.



Financial ratios are among financial statement analysis tool that are widely used in communicating financial performance of the firms. This study is conducted to investigate the initiative taken by companies in assisting the annual reports readers in understanding the financial performance of the firms. This initiative is considered as voluntary. Potential reason why companies provide this information is to portray in a simple way about their performance. This is helpful for unsophisticated readers of annual reports.

Further, by communicating financial ratios freely in the annual reports, potentially it will avoid additional cost being imposed to the users in order to get information about the firm. The information also is more reliable since it is provided in the company's official annual reports, as compared to third party financial information provider. It can be concluded that companies take voluntary initiatives in order to help investors and potential investor in understanding the firm's financial condition before making any investment decision. This initiative, indirectly increase the financial literacy of this group of financial information users.

Overall, the issue of financial literacy is not only the agenda of certain agencies such as Bank Negara, SIDC and Bursa Malaysia. Companies that provide annual reports to their stakeholders also can contribute to enhance the financial literacy of the interested parties. By providing simpler information, the complicated financial data of companies can be understood and utilised by category of users that have limited financial background.

In terms of the limitation, this study only considers ten (10) elements in the extent of financial ratio disclosures. A more comprehensive list of financial ratios should be investigated. Moreover, this study only consider one year (2011) as the period of study. Further, this study does not measure the usage of financial ratios from investors and potential investors' perspective. This study only focuses on initiatives provided by companies in helping these groups of stakeholders' understanding about performance of the companies. In addition, this study pick up the selected ratios as reported in the companies' annual reports, without comparing formulas between companies due to their unavailability. Some companies might use different formula for the same ratio with other companies, which cannot be traced in the annual reports. As long as the ratios presented in the annual reports matched with the list, it is considered as "disclosed".

In the future study, possibly a trend analysis may give more meaningful results. Government-linked and family companies; as well as small medium enterprises (SME) also could provide further insight. Using survey and interview techniques potentially contribute further about this unique financial reporting practice.

School of Accountancy
College of Business
Universiti Utara Malaysia
06010 UUM Sintok, Kedah
MALAYSIA

REFERENCES

Ali, S. (2013), *Financial literacy in Malaysia: Issues and status update*, Working paper presented at International Seminar on Financial Education and Retirement Savings, Kuala Lumpur, 17&18 September, 2013.

Atkinson, A. and Messy, F. (2012), *Measuring Financial Literacy: Results of the OECD / International Network on Financial Education (INFE) Pilot Study*, OECD Working Papers on Finance, Insurance and Private Pensions, No. 15, OECD Publishing.



- Abdullah, A., and Ku Ismail, K. N. I. (2008), Disclosure of voluntary accounting ratios by Malaysian listed companies, *Journal of Financial Reporting and Accounting*, 6 (1), 1-20.
- Botosan, C. A. (2006). Disclosure and the cost of capital: what do we know, *Accounting and Business Research*, 36 (Special issue), 31-40.
- Diamond, D. W., & Verrecchia, R. E. (1991). Disclosure, liquidity, and the cost of capital, *The Journal of Finance*, 46 (1), 1325-1359.
- Economic Transformation Programme (2010) (*source: www.etp.pemandu.gov.my*)
- Economic Transformation Programme Annual Report (2013) (*source: www.etp.pemandu.gov.my*)
- Evans, J. H., & Sridhar, S. S. (2002). Disclosure-disciplining mechanisms: Capital markets, product markets, and shareholder litigation. *The Accounting Review*, 77 (3), 595-626.
- Gibson, C. (1982). Financial ratios in annual reports. *The CPA Journal*, 52 (9), 18-29.
- Graham, J. R., Harvey, C. R., & Rajgopal, S. (2005). The economic implication of corporate financial reporting. *Journal of Accounting & Economics*, 40 (1), 3-73.
- Healy, P. M., & Palepu, K. G. (2001). Information asymmetry, corporate disclosure, and the capital markets: A review of the empirical disclosure literature. *Journal of Accounting and Economics*, 31 (1-3), 405-440.
- Ho, P. L., Aripin, N., and Tower, G. (2012). Corporate governance failure to influence the communication of key financial data over turbulent times. *Journal of Applied management Research*, 10(1), 1-18.
- Knauss, R. L. (1964). A reappraisal of the role of disclosure. *Michigan Law Review*, 62 (4), 607-648.
- Lang, M. H., & Lundholm, R. J. (1996). Corporate disclosure policy and analyst behaviour. *The Accounting Review*, 71 (4), 467-492.
- Lundholm, R., & Winkle, M. V. (2006). Motives for disclosure and non-disclosure: A framework and review of the evidence. *Accounting and Business Research*, 36 (Special issue), 43-48.
- Mitchell, J. (2006). Selective reporting of financial ratios in Australian annual reports: Evidence from a voluntary reporting environment. *Accounting Research Journal*, 19 (1), 5-30.
- Subramanyam, K. R., & Wild, J. J. (2009). *Financial statement analysis*. 10 ed. Boston: McGraw Hill.
- Watson, A., Shrikes, P., & Marston, C. (2002). Voluntary disclosure of accounting ratios in the UK. *British Accounting Review*, (4), 289-313.



A Review on Fraud

EMIE FAMIEZA BT ZAINUDIN

School of Maritime Business and Management

University Malaysia Terengganu

21030 Kuala Terengganu, Terengganu

MALAYSIA.

emiefamieza@gmail.com

HAFIZA AISHAH HASHIM

School of Maritime Business and Management

University Malaysia Terengganu

21030 Kuala Terengganu, Terengganu

MALAYSIA.

hafizaashah@umt.edu.my

Abstract

In the business community, fraud is an important topic which deserves attention, especially from vital stakeholders. Thus, this paper discuss types of fraud, how fraud occurs in terms of the fraud triangle, and its impact on the business and its shareholder. Generally, fraud requires three conditions: pressure, opportunity, and rationalizations. Using the real case of Transmile Group Bhd and Megan Media Bhd, fraud cases have shown that the issue is significant and has an impact on many stakeholders (Ruankaew, 2013).

Key words: fraud, fraud triangle, assets misappropriation, fraudulent financial reporting and corruption.

1. INTRODUCTION

In a firm or corporations, fraud receives attention from stakeholders including regulators, auditors, and members of the public (Higson, 2012). White collar crime and fraud is one of the top threats to American business (Ruankaew, 2013). Fraud is not easy, and detection requires knowledge about the nature of fraud and how it can be committed under concealment (Higson, 2012).



Based on a survey done by KPMG related fraud, bribery and corruption in 2013. The findings of the study show that, 89% of the survey respondents felt that the quantum of fraud has increased, while 94% of respondent believed that fraud have become more sophisticated. 85% of the respondents' opinions were that fraud is increasingly becoming industry-aligned and more targeted to certain business processes. 80% of the survey respondents also felt the incidents of bribery and corruption have increased in the last three years. The increase in fraud indicates that there is a strong need for further research.

We choose two registered Malaysian companies, namely Transmile Group Bhd and Megan Media Bhd, because of their fraudulent accounting activities. Furthermore, the two companies were involved in the biggest financial scandal in Malaysia, which was labelled as the cause of the financial scandals of Enron Mini Malaysia.

We have organized the balance of the paper as follows. The next sections discuss the definition of fraud, fraud triangle model, the type of fraud and the real case and impact of fraud in Malaysia. The final section will conclude this paper.

2. DEFINITION OF FRAUD

Fraud describes any act that intentionally deceives or misrepresents to others. Wrongful acts may be distinguished and defined in various ways; it is depend on the class of offenders. The legal meaning of fraud is stated as "A generic term, embracing all miscellaneous mean that human skill can devise, and forced by an individual to get an gain over another by false recommendations by destruct of truth and includes all surprise, trick, scheming, misleading, and any unfair way by which other cheated" (Mugala, 2013).

Per Chartered Institute of Management Accountants (CIMA), fraud basically involves deception to make a personal profit for themselves dishonest or cause a loss for the other party. Common fraud types includes activities such as theft, bribery, conspiracy, fraud, money laundering, bribery, and extortion (Doody, 2009).

Fraud is defined in many scholars and dictionaries. Serious Fraud Office (SFO) has defined fraud as abuse of position, or false representation, or prejudicing someone's right for personal gain. Based on the business dictionary, fraud as an act or acts of fraud, an intentional concealment, omission, or opposition to the

truth, to get the advantage of the law or unfair, encourage others to part with some valuable item or surrender a legal right, or imposes an injury in some way (<http://www.businessdictionary.com>).

Consequently, fraud may be defined as a deliberate act meant to encourage others to give up something of value or to surrender a legal right. It is a deliberate falsification or concealment of information to deceive or mislead.

3. FRAUD TRIANGLE



Figure 1: Fraud Triangle, source: (Higson, 2012)

Theory of fraud triangle consists of three essential elements of fraud (see figure 1). According to Dr. Yusof Nook (1993) and Joseph Eby Ruin (1996), there are three main causes of fraud as follows: (a) situational pressure on the individual, (b) opportunities to commit crime, (c) rationalization that allows to justify their illegal behaviour

To control fraud, business owners and executives must work on the fraud triangle. In the fraud triangle, the most important part is the opportunity to commit fraud. It may be difficult for management to do anything about it necessity or propriety of an employee, but by controlling the opportunities for fraud, companies can decrease it to some extent. Of the three elements, opportunity is the leg that organizations have the most control over. It is important that organization or firm develop processes, procedures, and controls should put employees in a position to effectively detect fraud and fraudulent activity if it occurs (Lacpa, 2012).

How fraud occurs in an organization can be understood by examining the elements in the fraud triangle. At an individual level, SAS No. 99 (Consideration of Fraud in a Financial Statement Audit) issued by the Auditing Standards Board has shown that fraud triangle consists of three conditions generally present when fraud (Day, 2010). These include incentives or pressures that provides a reason to commit fraud, the opportunity for fraud to be committed, and attitudes that allow individuals to rationalize fraud.



3.1 Pressure

Perceived pressures are associated with the motivations that lead to unethical behaviour. Some fraud perpetrators face certain pressure to commit unethical behaviours (Ruankaew, 2013). Pressure often involves a non-sharable financial need. Management of an organization usually feel pressured to commit fraudulent activities due to poor cash position, loss of customers and market decline.

A firm can provide incentives to manipulate income, when any one of the three following conditions occur. First, financial stability is threatened by the economic crisis and the problems of the industry, secondly, the management or owner of a firm is stress to meet the expectations of third parties and finally the financial situation where the management or directorship is intimidated by entity's financial performance (Yung-I Lou, 2009).

Based on the earning threshold, there are three hierarchies: (1) to avoid negative earnings; (2) reporting an increase in quarterly earnings; and (3) achieving earnings forecasts (Degeorge, 1999). Based on Kasznik and McNichols (2002) abnormal returns were significantly for firms to meet analysts' expectations after controlling for analysts' expectations of future earnings, and also the unusual market punished firms without expectations. To achieve earning forecast, this situation imposed pressure on management expectation. Lopez and Rees (2002) demonstrated that earnings multiples used for unexpected income is greater than that for the unexpected negative income. The pressure exerted on management to meet analyst earnings estimates is the main cause of fraudulence. Dechow et al. (1996) argued that firms with high debt leverage have motivational to manipulate of income.

3.2 Opportunities

Opportunity is the second element of the fraud triangle. Opportunities may be defined as a mechanism or position in which potential scammers use their position to solve their non-shareable financial needs. Opportunities need be considered personal risk is low, which means that they trust that the misconduct will remain confidential.

Opportunity is a situation which provides an opportunity for organisation or upper level to implement material amount misstatement in the financial report. Opportunities that can lead to fraudulent financial statements may include weak or non-existent internal controls, the absence of an audit committee that is correct, errors not justified by the Board of Directors, and the organizational structure of the complex.



Jensen (1993) argued for the separation of the office of chairman of the board of the Chief Executive Officer (CEO) if the board is a monitoring tool, because as chairman of the board conducted a meeting of the board of directors and oversee the process of hiring and evaluation and compensation of the Chief Executive Officer.

3.3 Rationalisation

Rationalisation is the last element of the fraud triangle model. According to a study conducted by Cressey most people who commit fraud have no criminal convictions before and do not see themselves as a criminal, but as a victim of surroundings (Day, 2010). As there is no standard training of fraudster, the model can apply equally well to anyone from director to employees; indeed, the majority of the cases Cressey studied involved either of these as he was reviewing misappropriation. This means that the need to find some way in which the scammers can rationalize their actions to themselves that they are not criminal in their own minds (Day, 2010).

Rationalization is the ability to act based to ethical values and code of conduct. To make their actions seem acceptable, fraudsters find a way to rationalise their action. Besides, to meet the goal of a company, the management may consider fraud financial statements only competing with other organizations. Usually, top-level managers can rationalize their actions because they try to protect shareholders by manipulating financial reports. By manipulating financial statement, share price reaction will increase.

4. TYPES OF FRAUD

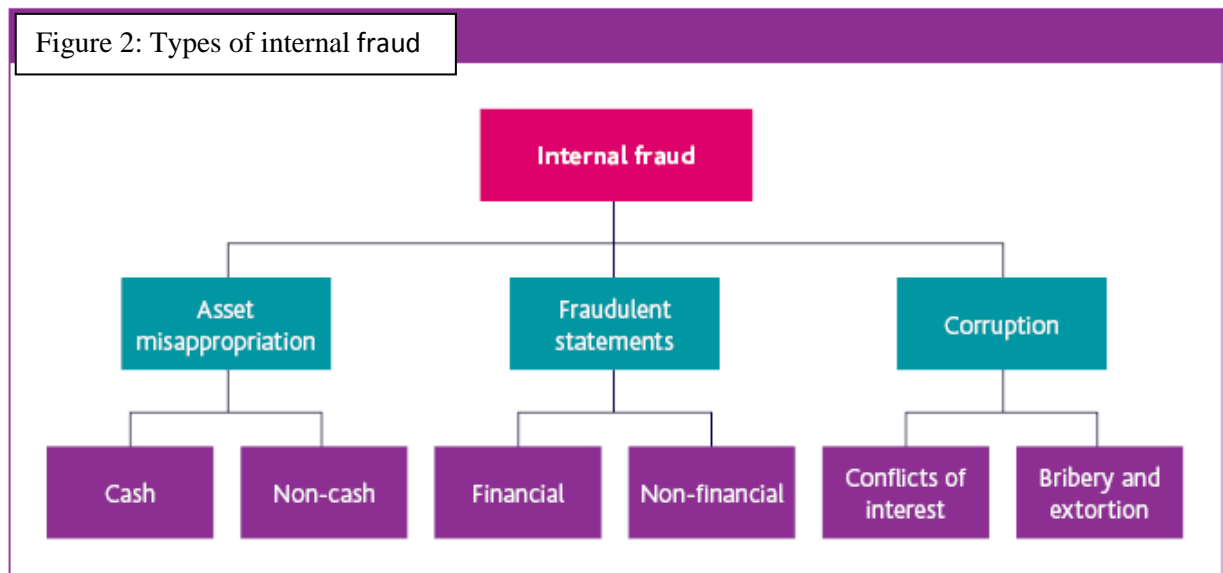
There are many types of corporate fraud. In many fraud schemes, more than one type of fraud is present. Common frauds are as follows (Doody, 2009):

- Theft of cash, physical assets or confidential information
- Accounts abuse
- Procurement fraud
- Fraud of payroll
- Financial accounting misstatements
- Inappropriate journal vouchers
- Accounting fraud suspense
- Fraud reimbursement of expenses
- False employment eligibility
- Bribery and corruption

In a firm or organisation, fraud may come in many circumstances and events. Fraud has different names including internal fraud, employment fraud, or dishonesty of employees. There are three basic types of fraud: asset misappropriation, bribery and corruption, and fraudulent financial statements. CIMA classified these three basic of fraud under internal fraud. Three main categories of internal fraud affect an organization (Doody, 2009). Figure 2 summarises types of internal fraud.

The three categories of internal fraud are:

- ✓ Assets misappropriation
- ✓ Fraudulent financial reporting
- ✓ Corruption



Source: (Doody, 2009)

Assets misappropriation

Asset misappropriation in fraud involves the theft of an entity's assets. In many cases, the amount involved are not material to the financial statement. However, the loss of the company's assets is an important management concern, and the materiality threshold for fraud management may be much lower than the materiality threshold used by an auditor for financial reporting purposes (Arens et al., 2010).

Common features include the theft of cash or other assets of the company, for example (Doody, 2009):

- Cash theft - The physical theft of cash, such as theft of petty cash from the company's premises.
- Fraudulent disbursements – Company funds being used to make fraudulent payments. Typical examples include billing schemes, where payments are made to suppliers to a fictitious supplier, while in salary schemes, payments made to employees are faked.



- Inventory frauds - Taking inventory from the store or company for personal use.
- Mismanagement of assets - Employees use company assets for their own individual interests.

Fraudulent financial reporting

In general term, fraudulent financial reporting can be defined as an intentional misstatement or omission of amount or disclosure with the intent to deceive the users. However, most cases of fraudulent financial reporting involve the intentional misstatement of amounts and not disclosure.

Based on auditing perspective, fraudulent financial reporting is a deliberate attempt to deceive or mislead users of financial statements by providing and disseminating materiality misstated financial statements, especially to investors and creditors. Financial reporting fraud involving fraudulent intent and deception by a clever team of knowledgeable as like top executives and auditors with a set of planned schemes (Rezaee, 2005). Fraudulent financial reporting may involve the following criteria: (1) alteration, falsification, or manipulation of financial records, supporting documents, or other business transactions; (2) intentional misrepresentation, omission, or misrepresentation of events, transactions, accounts, or other important information from financial statements; (3) Mistakes intentionally, deliberately misinterpreted, and illegal accounting standards, philosophies, rules and methods used for the measurement, recognition, and reporting of economic events and business activities; (4) omission or presentation and disclosure of adequate disclosure on accounting standards, principles, practices, and related financial information; (5) aggressive accounting techniques through management of illegal procedure; and (6) manipulation of accounting practices under accounting standards based on existing rules that have to be too detailed and too easy to intercept and contain loopholes that allow companies to hide the substance of their performance (Rezaee, p.279,2005).

The study by (Firth et al., 2011) showed that a high ratio of debt to equity in the business to which the agreement is a contract between the factors that influences managers to falsify their financial statements. Most case of fraudulent financial reporting involves the intentional misstatement of amount, not disclosures (Rezaee, 2005). Omissions of amount are less common, but the company may overstate income by leaving accounts payable and other liabilities (Arens, et al., 2010). Although most cases of fraud involving overstate of assets and income or omissions of liabilities and expenses in order to over record earnings, it is important to note that companies often manipulate by understating income (Belinna, 2008).

Erosion in the financial reporting quality is perceived to be related with financial reporting irregularities such as fraudulent financial reporting and financial restatement (Hashim, 2014). Based on a statement by Zarinah Anuar as Chairman of Malaysia Securities Commission, 2007 “Financial statements as the main medium or references for shareholder to make their decisions whether to invest or not in a company.



Therefore, the quality of financial statement is important to investor. If the auditors unable to prepare quality audit reports, investors, exposure to misstated financial statements and financial statement fraud will remain” (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013)

Corruption

Fraud corruption can divided into three types: conflict of interest, bribery, and extortion. Studies show that corruption is involved in about one-third of all fraud. In the conflict of interest fraud, scammers have their influence to achieve personal gain cause affecting the company. Fraudsters do not get financial benefits, but receive improper personal benefits as a result of circumstances. For example, a manager can approve the expenses of an employee who is also a personal friend to maintain a friendship, even though spending is not accurate. Bribery is when money or something else of value is offered to influence the situation. Extortion is against corruption, and occurs when the money requested is not offered to guarantee specific results (Weaver, 2008).

Based on the survey by KPMG in 2013, the most common factors that contribute to unethical behaviour include poor communication of organizational values or code of conduct. There is also the factor of corruption for weak internal controls, followed by the Internal Audit team skills shortage and lack of awareness to detect fraud. The Serious Fraud Office (SFO) has said that corruption occurs in which the integrity of the person, government or company is manipulated and compromised for their own personal gain.

5. IMPACT OF FRAUD

The fraud consequences will adversely affect towards credibility, integrity, and transparency of financial statement quality. Shareholders may use the financial statements as a strategic device to decide whether to invest in the company or not. Therefore, people involved in financial statement fraud will destroy careers. Consequently from fraud, this makes the capital market and economic growth less efficient. At last, they cause bankruptcy of firm and less efficient. When this happens, it will encourages regulatory intervention, and less public confidence level and trust in accounting and auditing profession (Vlad, Tulvinsshi & Chirita, 2011).

Companies which engage in some practice like accounting irregularities and earning management may collapse. This happen because the market reaction decrease and they did not maintain completion with other organisations. Corporate collapse has been listed as a factor for bankruptcy (Day, 2010).



For this paper, we choose Transmile Group Bhd and Megan Media Bhd as a listed companies in Malaysia. Both companies have been labelled as the cause of the financial scandals of Enron Mini Malaysia, because the largest reported in Malaysia and it also involved higher level people of the company (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013).

In the section 5.1 and 5.2 review the history of both Malaysia mini Enron case:

5.1 Transmile Group Bhd

Transmile Group Bhd is a cargo airline was incorporated in 1993 and had a head office Subang Selangor, Malaysia. Express air cargo is the main activity of the company, for which it has obtained landing rights in the countries of Asia-Pacific. It has courier transportation and the service international company such as the local Pos Malaysia Bhd, Nippon Express, DHL Worldwide Express, and United Parcel Service. In addition, aviation maintenance as well as other related business activities operated by a subsidiary (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013). As the largest shareholder of the company was a billionaire and one of the famous local investment arms of the state was the second largest shareholder, it was under the scrutiny of analysts and institutional investors. In 2006, the company was voted among the 200 small midsize companies by one well-known business publication.

Early warning signals for fraudulent accounting activities of this business has been seen by the public when the company unable to submit within the due date for the 2006 annual report to the stock exchange in April 2007. External auditors refused to sign the report because they failed to get supporting document for related transactions of business such as the movement of plant and equipment in the company and its subsidiaries. For financial statements ending December 2006 and 2005, Transmile Group Bhd also overemphasised its group's revenue by 30% and 35% of the consolidated revenue (Puteh Salin, Kamaluddin, & Abdul Manan, 2011). Earlier, in February 2007, the Board approved the unaudited results showed an 80% increase in revenue, net profit doubled, and trade receivables increased to RM381 million from RM111 million in 2005 (Fong, 2007). A day before, the audit committee meeting highlighted a number of issues in the accounts; however, the issue was not raised at the meeting of the board on the following days. This was because the audit committee also involved in fraud case.

Per The Star Online on 31 May 2007, new board appointed to lead a specific audit of the accounts company (Fong, 2007). According to preliminary findings of a special audit of the annual audited accounts, Transmile Group Bhd's revenue for the financial year ended Dec 31, 2005 and 2006 may have been overstated by a total of RM530 million (Fong, 2007). In addition, RM341 million in property, plant and equipment account seems to have been designed as a number that is not much supported by documents (Zaimee, 2007). In



addition, the company is also alleged to have made payments amounting to RM189 million, without any support document (Zaimee, 2007). During a special audit, more than RM103 million was found in the accounts of the subsidiary account related to party transactions in which the subsidiary owed to the business (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013).

Newly appointed directors had a police report on the earning management about income, property, plant and equipment, and payments to other parties. Then, the former CEO, founder, and ED was imposed by the court because of submitting misleading the financial statements (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013). Furthermore, the two former independent director and members of audit committee have been found a mistake for the release allow ambiguous financial statements to the stock exchange. This was the first case in Malaysia to charge the independent directors and signaled to the market that independent directors cannot endorse everything given to them.

In July 2007, the company made an announcement regarding the bailout of the subsidiary companies as liabilities larger group and ultimately the shareholders lose their investments from a large fall in its stock market, which was the highest on January 3, 2007 at RM14.40, to RM4.64 on July 3, 2007 and below RM0.50 since March 2010 (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013). Finally, the company was delisted from the stock exchange on March 2011. In addition, shareholders equity declined from RM424 million to a negative of RM289 million in 2007 and RM1.2 billion loss in market capitalization (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013)

5.2 Megan Media Bhd

Megan Media Bhd was incorporated in 1994. The main activities of the company and its subsidiaries are the manufacture of electronic data storage, such as diskettes, video tapes, and recordable discs. In April 2007, alert accounting irregularities became public knowledge, when two of its subsidiaries fail to pay for all their trading facility maturing obtained from a local bank, amounting to RM893.97 million.

To regularize its financial position, the company proposed a debt restructuring plan. Thus, the bank asked the company to hire a forensic auditor to lead a fact finding into the account of the company. Preliminary findings found irregularities in the accounts of the subsidiary companies of trade receivables and creditors a total RM456 million. In addition, the auditors found that the subsidiary had financed the payment of trade payables design through lending and cash recycling through another business entity and proof of the payment made to the creditor does not exists using bank facility. Further investigations revealed other accounting



irregularities, such as the illegal figure of RM211 million for the payment of an asset to the production line in a subsidiary (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013).

Securities Commission initiated an investigation into the account of the company after the announcement of the third quarterly report. In December 2007, Executive Chairman, Executive Director and Financial Controller of the company charged the commission because of wrong income figures given (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013):

- The year ended 30 April 2006 about RM1.03 billion reported in its consolidated accounts;
- The financial period ending 31 July 2006 about RM 230 million in its consolidated quarterly report;
- The financial period ending 31 October 2006 about RM238 million in its consolidated quarterly report; and
- The financial period ending 31 January 2007 about RM306 million in its consolidated quarterly report;

Per the report above, a significant figure of income the past have been wrong report, so it did not submit the regularization plan. For the year ended 2007, the company had a net loss of RM1.27 billion. Besides, the company also have negative cash flow RM897 million. Thus, the firm could not sustain financial health and was unlisted in April 2008. Over a period of three months after the news went public, shareholder losses reached 85% as the company shares slid from RM0.60 to RM0.04 (Abdul Hamid, Shafie, Othman, Wan Hussin, & Fadzil, 2013).

6. CONCLUSION

This paper has reviewed the types of fraud that can be significantly affect business. The cost of fraud is estimated to be relatively high and is rising steadily (Ruankaew, 2013). In order to successfully address fraud, it is critical for businesses to understand the behavioural root causes of fraud. From that fraud triangle model, we may identify factors why fraud occurs in a company or organisation based on the three element of the fraud triangle.

This study reviews the real case which is Transmile Group Bhd and Megan Media Bhd which has been labeled as the cause of the financial scandals of Enron Mini Malaysia. The results showed that the top level management involvement of may be caused by self-indulgence, weaknesses in corporate governance regulation, and lower penalties imposed under the law existing. We have determined three factors that potentially for why two companies involved in the fraudulent accounting activities: (a) situational pressure on



the individual; (b) opportunities to commit crime; (c) rationalization that allows people to justify their illegal behaviour.

Despite presenting a serious risk of fraud by businesses, many organizations still do not have formal systems and procedures to prevent, detect, and respond to fraud. No system is really foolproof, but businesses can take steps to prevent fraud and make it less attractive to do so. Management accountants, professional training which includes information and analysis system, has an important role to play in developing and implementing anti-fraud measures within their organizations.

Acknowledgements

We acknowledge the Ministry of Education Malaysia for the grant that assisted this research (Vote No.59302)

References:

A) Book

Arens, A. A., Elder, R. J., Beasley, M. S., Amran, N. A., Fadzil, F. H., M Yusof, N. Z., et al. (2010). *Auditing and assurance services in Malaysia*. Prentice Hall.

B) Website

Bursa Malaysia. (n.d.). Retrieved June 24, 2014, from <http://www.bursamalaysia.com/corporate/>

BusinessDictionary. Com. (n.d.). Retrieved September 26, 2014, from <http://www.businessdictionary.com/definition/fraud.html>

Coenen, T. (n.d.). *All Business Network*. Retrieved September 26, 2014, from <http://www.allbusiness.com/crime-law-enforcement-corrections/criminal-offenses/6635361-1.html>

Serious Fraud Office. (2014). Retrieved September 26, 2017, from <http://www.sfo.gov.uk/fraud/what-is-fraud.aspx>

The Fraud Triangle(What can you do about it). (n.d.). Retrieved July 10, 2014, from <http://www.lacpa.org.lb/Includes/Images/Docs/TC/TC363.pdf>

Tessier, D. R. (2013, October 29). *The Fraud Triangle Theory How a three-pronged approach can improve your bottom line*. Retrieved June 18, 2014, from Claims Management Strategies For Successful Resolutin: <http://claims-management.theclm.org/home/article/Insurance-fraud-triangle-theory>

C) Article



- Abdul Hamid, F., Shafie, R., Othman, Z., Wan Hussin, W., & Fadzil, F. H. (2013). Cooking the Books: The Case of Malaysian Listed Companies. *International Journal of Business and Social Science*, 179-186.
- Alvin A. Arens, R. J. (2010). *Auditing and Assurance Services in Malaysia*. Malaysia: Pearson Malaysia.
- Day, R. (Vol. 5, no. 1 (2010)). Applying the Fraud Triangle Model to the Global Credit Crisis. *Iceland E-Journal of Nordic and Mediterrian Stusies*, 1-33.
- Doody, H. (2009, May). *Chartered Institute Management Accountant*. Retrieved September 30, 2014, from Corporate Fraud.
- Firth, M., Rui, O. M., & Wuc, W. (2011). Cooking the books: Recipes and costs of falsified financial statements in China. *Journal of Corporate Finance*, 17, 371-390.
- Fong, K. (2007, May 31). Transmile's revenue may have been overstated, special audit finds. Malaysia, Petaling Jaya.
- Hashim, A. M. (Vol. 5, No. 2, April 2014). Accounting Irregularities in Related Party Transactions. *International Journal of Trade, Economics and Finance*, 181-183.
- Hashim, H. A. (2014). *Corporate Board Composition, Expertise and Earning Quality*. Kuala Terengganu: Penerbit UMT.
- Hawariah Dalniah, A. K. (2014). Detecting Fraudulent Financial Reporting through Financial Statement Analysis. *Journal of Advanced Management Science Vol. 2, No. 1*, 17-22.
- Higson, R. K. (2012). The New Fraud Triangle Model . *Journal of Emerging Trends in Economics and Management Sciences (JETEMS)* 3(3), 191-195.
- Jerry L. Turner, T. J. (2003). *An Analysis of the Fraud Triangle*. California.
- Mariana VLAD, M. T., & Chirita, v. T. (2011). *THE CONSEQUENCES OF FRAUDULENT FINANCIAL REPORTING*. Romania: The Annals of The "Ștefan cel Mare" University of Suceava. Fascicle of The Faculty of Economics and Public Administration.
- Mugala, J. (2013, February 8). *National Social Security Fund & Anor v Alcon International Ltd*. Retrieved September 30, 2014, from Uganda Legal Information Institute: <http://www.ulii.org/ug/judgment/supreme-court/2013/4>
- Puteh Salin, A., Kamaluddin, N., & Abdul Manan, S. (2011). Unstoppable Fraud, Scandals and Manipulation – An Urgent Call for an Islamic-based Code of Ethics. *International Conference on Sociality and Economics Development IPEDR vol.10 (2011) © (2011) IACSIT Press, Singapore*, 474-478.



- Rezaee, Z. (2005). Causes, consequences, and deterrence of financial statement fraud. *Critical Perspective on Accounting* 16 , 278-296
- Ruankaew, T. (2013). The Fraud Factor. *International Journal of Management and Administrative Sciences (IJMAS)*, 1-5.
- Serving UC Merced through Stewardship, Accountability and Excellence.* (n.d.). Retrieved June 18, 2014, from The Fraud Triangle: <http://controls.ucmerced.edu/fraud-triangle.aspx>
- Weaver, L. (2008). *Forensic auditing*. Malaysia: ACCA.
- Yung-I Lou, M.-L. W. (February, 2009). Fraud Risk Factor Of The Fraud Triangle Assessing The Likelihood Of Fraudulent Financial Reporting. *Journal of Business & Economic Research*, 61-78.
- Zaimee, A. (2007, July). *Mini-ENRON'S SHAKING UP Malaysia's Corporate Governance?* Retrieved September 30, 2014, from Accountant Today: <http://www.mia.org.my/at/at/200707/06.pdf>

EMIE FAMIEZA BT ZAINUDIN

School of Maritime Business and Management
University Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA.

HAFIZA AISHAH HASHIM

Lecturer
School of Maritime Business and Management
University Malaysia Terengganu
21030 Kuala Terengganu, Terengganu
MALAYSIA

The Relationship between Intensity of Competition, Delegation of Authority, Management Accounting and Control Systems Changes, Organizational Performance (Empirical Study in Manufacturing Companies Listed in Indonesian Stock Exchange)

Lukluk Fuadah, SE. MBA, Akt.
Economics Faculty, University of Sriwijaya, Palembang.
Jl. Raya Prabumulih-Indralaya 30662, Indralaya
(+62711) 580964, 580646 Fax (+62711) 580646
lukluk.asmawi@gmail.com

Prof. Muhammad Nasir, MSi, Ph.D, Akt
Dr. Jaka Isgiyarta, MSi, Akt
Jl. Prof. Sudarto, SH. Tembalang Semarang. 50275
(+6224) 76486851, 76486853 Fax (+6224) 76486852
Faculty of Economics and Business, University of Diponegoro,
mnasirundip@yahoo.com; jaka_isgiyarta2@yahoo.com

Abstract: *The aim of this study is to investigate the relationship between intensity of competition and organizational performance through delegation of authority, changes in management accounting and control systems. Data of this study was collected from survey to chief financial officers or controller or accounting manager from manufacturing companies listed on the Indonesian Stock Exchange. From 477 questionnaires were distributed and 115 respondents were returned, only 108 respondents used in data analysis. This study used Structural Equation Model (SEM) by using AMOS 19 program software. The findings from this study showed that the intensity of competition and organizational performance was not significance. However, other results from the relationship among intensity of competition, delegation of authority, management accounting and control systems changes, and organizational performance have positive relationship and significance.*

Keywords: *Intensity of Competition, Delegation of Authority, Management Accounting and Control Systems, Organizational performance.*

1. INTRODUCTION

This study replicates the model developed in Hoque's (Hoque, Z. 2011. The relations among competition, delegation, management accounting systems changes and performance: A path model. *Advances in Accounting*, Vol. 27, No. 2: 266-277). Hoque's empirical investigation into the relations among competition, delegation, management accounting and control systems (MACS) changes and organizational performance. It follows a standard contingency type path modeling to propose that intensity of competition causes firms to change their MACS and that this change enhances their performance. This study used two theories including organizational theory and contingency theory.

The aim of this study is to investigate the relationship between intensity of competition, delegation of authority, changes in management accounting and control systems- MACS, and

organizational performance in Manufacturing Companies Listed in Indonesian Stock Exchange. In globalization, manufacturing companies face higher competition from other countries especially after ASEAN Free Trade Area (AFTA) on 2004. As a one of ASEAN countries, manufacturing companies in Indonesia face higher competition. It is important to investigate the role of changes in management accounting and control systems in manufacturing companies listed in Indonesian Stock Exchange.

2. LITERATURE REVIEW

2.1. The relationship between intensity of competition and delegation of authority

Market competition is one of key element from company's external environment (Krishnan 2005); (Krishnan et al. 2002); (Libby & Waterhouse, 1996); (Mia and Chenhall, 1994). Intensity of competition has big influence in internal organization (Khandwalla, 1972); (Lawrence and Lorsch 1967). Galbraith (1977) stated that external variable is uncertainty environment for instance intensity of competition. Galbraith (1977) also explained that companies have multiple responds for uncertainty environment, one of these is to delegate their authorities.

Based on organizational theory, in competitive environment tend to delegate authority from senior managers to lower managers (Burns and Stalker, 1961) dan (Chandler, 1962). In organizational theory has premised that environment has relationship with organization structure (Gordon and Narayanan, 1984). From previous researchers such as Prendegast (2002), Waweru, (2008), dan Waweru and Uliana (2008) found that there is a positive relationship between intensity of competition and delegation of authority. This idea is formally expressed in the following hypothesis:

H1: Intensity of competition has positive relationship with delegation of authority.

2.2. The relationship between intensity of competition and Management Accounting and Control Systems Changes (MACS)

Contingency Theory stated that company more effective if management control system was designed suit with contextual variables such as uncertainty environment for example intensity of competition. From management accounting literature environment is one of factor determine design of management accounting and control systems that useable for company (Ezzamel 1990); (Gordon and Miller 1976).

Based on proposition (Chenhall 2003) described that the more uncertain the external environments, the more open and externally focused on management control systems. Prior researches that used contingency theory explain that firms today need changes in management accounting and control system due to higher competition Khandwalla (1972), Mia (1993), Mia and Chenhall (1994), Libby and Waterhouse, (1996), Mia and Clarke, (1999), Hoque et al. (2001), Williams and Seaman, (2001), Baines and Langfield Smith, (2003), Waweru et al. (2004), Krishnan (2005), Isa et al. (2005), Agbejule and Burrower (2007), Abdel-Kader and Luther (2008), Tuanmat et al. (2010), Hoque, (2011), Hammad et al. (2013), Mohamed (2013). In conclusion, the prediction that increased competition is likely to lead a firm to increase of changes in management accounting and control systems, this idea is formally expressed in the following hypothesis:

H2: Intensity of competition will be positively associated with changes in management accounting and control systems.

2.3. The relationship between Delegation of Authority and Changes of Management Accounting and Control Systems (MACS)

Decentralization in the organization can provide greater control and responsibility for managers in the activities and require a larger type of information (Waterhouse and Tiessen 1978). Moreover, delegation of authority creates the opportunity for lower-level managers to changes their MACS (Abernethy and Bouwens 2005). Thompson, (1967) also stated that due to the spread of decentralized decision-making authority within the business units delegation raised a tendency towards innovation. This implies that the increased delegation of authority, require changes in MACS. Furthermore,

Kaplan and Atkinson (1998) revealed that managers need reliable information about their products and services so that appropriate decisions can be made to meet local needs.

Gul and Chia (1994), Abernethy and Bouwens (2005), Waweru, (2008), Waweru dan Uliana, (2008), Soobaroyen and Poorundersing (2008), Chenhall (2008), Abdel-Kader dan Luther (2008), Verbeeten, (2010), Ajibolade (2013), Hammad et al. (2013) showed that a positive relationship between decentralization and MACS changes. This idea is formally expressed by the hypothesis is as follows: \

H3: Delegation of authority is positively associated with changes in Management Accounting Control System.

2.4. The relationship between delegation of authority and organizational performance

More delegation provides incentive to lower manager to make economical decision and result in increasing organizational performance (Prendergast, 2002). With Delegation of authority, local or lower managers may respond timely to their local customers and they do not have to wait for approval from a higher authority for business decisions.

Based on Chenhall, (2003) and Otley, (1980) stated that contingency theory from management accounting if organization use management accounting and control systems fit in organization factors such as decentralization have better performance. Previous researches showed that there is a positive relationship between delegation of authority and organizational performance (Manfield and Alam 1985), (Miah and Mia 1996), (Danersen 2001) dan (Hoque, 2011). Based on explanation above, it can be develop a hypothesis as follow:

H5: Delegation of authority has positive associated with organizational performance.

2.5. The relationship between Management Accounting and Control Systems changes and organizational performance

Changes in management accounting and control systems allow managers to obtain information needed for successful economical decision making (Chenhall and Morris, 1986); (Mia and Chenhall, 1994). Contingency theory of management accounting suggests that companies are likely to have high performance if they implement and use management accounting and control systems that suit their social environmental situations and organizational (Chapman 1997); (Chenhall 2003); (Chenhall and Chapman, 2006); (Otley 1980). Based on contingency theory stated that how greater use of management control system was a response to interdependence and this information assisted in maintaining high performance (Chenhall 2003).

There is also an increasing recognition in the literature of management accounting that companies tend to apply the accounting innovation or changes in management accounting control system which exists to enhance the decision making as well as the performance of the company (Abernethy and Bouwens, 2005). Prior studies showed that changes in management accounting and control system is associated with organizational performance for example (Mia and Chenhall 1994); (Mia and Clarke 1999); (Williams and Seaman 2002); (Ismail and Isa 2011) and (Hoque 2011). In conclusion, it can be developed a hypothesis as follow:

H5: Management accounting and control system changes will be positively related to organizational performance.

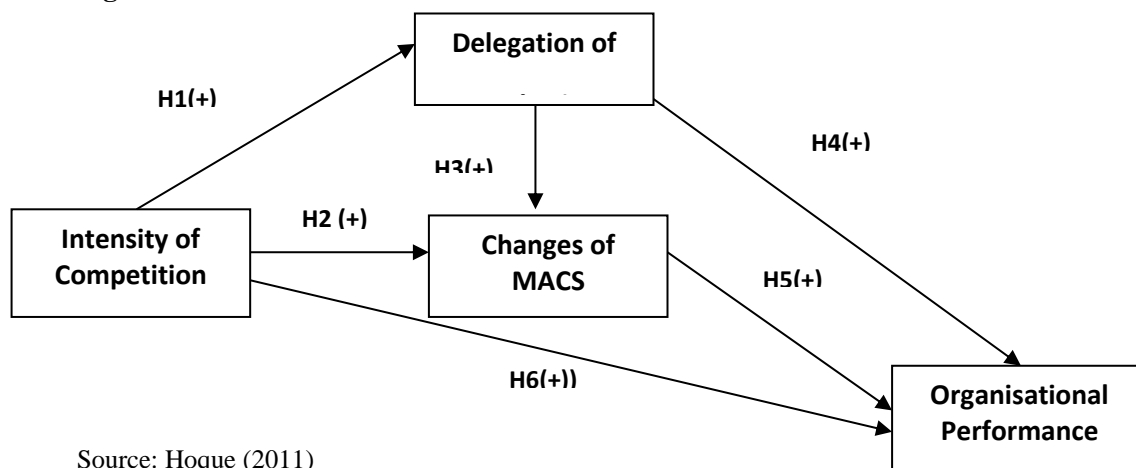
2.6. The relationship between intensity of competition and organizational performance

Contingency theory from management accounting explains that if a company use management accounting system that appropriate with organizational and environment factor that tend to give better performance (Chenhall, 2003); (Otley, 1980). This relationship was explained with contingency theory that mentioned that management accounting practices and internal operation from organization fit in with external environment changes (Abdel-Kader and Luther 2008); (Haldma and Lääts 2002); (Macy and Arunachalam 1995).

Prior researches from Govindarajan (1984), Mia and Clarke, (1999) and Hoque, (2011) showed that there is positive relationship between intensity of competition and unit business performance. However the result study from (Khandwalla 1972) showed that intensity of competition had negatively associated with organization performance. The above discussion suggests that the increase of intensity of competition, the increase organization performance should also increase. Stated formally in the form of the following hypothesis:

H6: Intensity of competition has positive relationship with organizational performance.

Figure 1. Research Model



Source: Hoque (2011)

3. METHODOLOGY

3.1. Population and Sample

Participants of this study are financial controller or chief financial officer or accounting managers. The amount of manufacturing firms which listed in Indonesian Stock Exchange is about 149 based on Indonesian Capital Market Directory. The questionnaires were sent to all manufacturing companies. Sample in this study was the total completed questionnaires returned from survey. Data was collected by sending questionnaires by mail and contact persons who sent directly to manufacturing companies that listed in Indonesian Stock Exchange.

The reasons choose manufacturing companies as sample. Firstly, because manufacturing companies in Indonesian Stock Exchange especially from Indonesian Capital Market Directory is categorized as a big company (Lau and Sholihin 2005). These companies tend to use Management Accounting and Control Systems. Other reason is to avoid bias from Industrial effect.

3.2. Variable Research and Instrument Research

3.2.1. Intensity of competition

This variable used Khandwalla (1972) measurement which has five categories such as raw materials, technical personnel, selling, and distribution, quality and variety of product and price. Several researchers used this measurement (Mia and Chenhall 1994); (Libby and Waterhouse 1996); (Hoque et al. 2001).

3.2.2. Delegation of Authority

Definition of decentralization of authority is refer to senior manager delegate to lower level managers (Libby dan Waterhouse, 1996). Authority is act related to decision without confirmation from senior level managers (Hoque, 2011).

3.2.3. Changes of Management Accounting and Control Systems

Libby and Waterhouse (1996) developed management accounting and control system changes measurement. This measurement consist of twenty three items which divide into five categories of planning, controlling, costing, directing and decision making. This measurement was used by several studies (Libby and Waterhouse 1996); (Williams and Seaman 2001); (Williams and Seaman 2002); (Sulaiman and Mitchell 2005); (Isa 2007); (Isa 2009); (Verbeeten 2010); (Ajibolade et al. 2010).

3.2.4. Organizational Performance

Organizational performance is indicator successful level to achieve company goal. Govindarajan, 1984 states that organizational performance is not only financial but also non financial performance in the company. This instrument was developed by (Govindarajan 1984). This measurement consists of ten categories such as operating profit, return on investment, sales growth rate, market share, cash flow from operation, new product development, market development, research and development, cost reduction programs, personnel development. already used by several researchers such as (Abernethy and Stoelwinder 1991); (Chenhall and Langfield-Smith 1998); (Govindarajan and Fisher 1990); (Hoque and James 2000), Hoque (2011).

3.3. Analysis

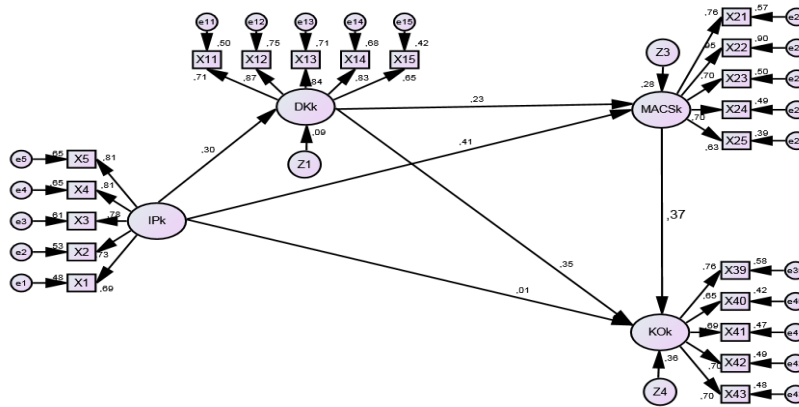
Data analysis used Structural Equation Model (SEM) with AMOS (Analysis of Moment Structure) 19 software program. Structural Equation Model (SEM) is the combination between factor analysis and all equation model (Ghozali 2011). Structural equation is figured by path diagram that represent from theory. In other word latent variable is figured out to path diagram from theory. Furthermore, goodness of fit model is will done. If it is fit, it will explain the result and discussion (Ghozali, 2011).

4. EMPIRICAL RESULT

Total questionnaires were about 447 questionnaires which were sent to financial controllers or chief financial officers or accounting managers (each firm is sent 3 questionnaires). The questionnaires were distributed in early September 2012 until mid February 2013. The total resulted in only 115 completed responses. Of 115 returned questionnaires, seven (7) responses were not fully completed and therefore were not useable. Thus, the usable response for this study analysis is about 108.



Figure 2. The Result Research from AMOS



Chi Square = 238,759
 Probabilitas = ,000
 CMIN/DF = 1,456
 GFI = ,829
 AGFI = ,781
 TLI = ,920
 CFI = ,931
 RMSEA = ,065

Table 1. Goodness of Fit Model

Goodness of Fit Indexes	Cut off Value	Result	Model Evaluation
Chi-Square (df = 266)	(< 305,041)	238,759	Good
Probability	≥ 0,05	0,000	Good
RMSEA	≤ 0,08	0,065	Good
GFI	≥ 0,90	0,829	Marginal
AGFI	≥ 0,90	0,781	Marginal
CMIN/DF	≤ 2,00	1,456	Good
TLI	≥ 0,95	0,920	Good
CFI	≥ 0,95	0,931	Good

Table 1 showed that all the evaluation of goodness fit indexes were good, except for GFI and AGFI are categorized in marginal level. The goodness fit of model based on the criteria (cut off value). Chi square from full model result is smaller than chi square table as 305,041. All values are required range which means that all indicator was used in model is sufficient enough to test the hypothesis.

Table 2. Standardized Result of Structural Equation

Dependent Variable	Independent Variable	Hypothesis	Direction of Hypothesis	Estimated Standard	C.R.	P	Explanation
DKk	IPk	H1	+	0,295	2,595	,009	Suppoted
MACSk	IPk	H2	+	0,414	3,650	***	Suppoted
MACSk	DKk	H3	+	0,233	2,292	,022	Suppoted
KOk	DKk	H4	+	0,354	3,153	,002	Suppoted
KOk	MACSk	H5	+	0,370	2,996	,003	Suppoted
KOk	IPk	H6	+	0,014	0,122	,903	Not Supported

IPk = intensity of competition, DKk = delegation of authority, MACSk = changes in management accounting and control systems, KOk = organizational performance.

Table 2 showed that all hypotheses are accepted or supported, except for the relationship between intensity of competition and organizational performance is not supported. The finding of this study confirm the argument and support in organization theory which states that the environment of high competition emphasizes top managers or senior managers to delegate more authority to lower level managers (Burns and Stalker, 1961; Chandler, 1962). This is because local managers or lower level managers more aware of the actual conditions that exist on a local company with more detail. In addition, lower level managers making decisions quicker and better. This is done to respond to the competition included in an uncertain environment so as to respond to the uncertainty will be delegation of authority. This finding is not support to Hoque's finding.

The finding of this study confirm the basic premise of contingency theory (states that the company will be more effective if the management control system designed in accordance with contextual variables such as environmental uncertainty is an example of the intensity of competition. The environment is one of the factors determining the design of management accounting control systems which are used by the company based on the literature of management accounting and control, (Ezzamel, 1990), (Gordon and Miller, 1976). This result indicates that increased competition is positively related to the greater number of MACS changes, this finding support to Hoque (2011).

This finding supports the contingency theory which states that decentralization is the delegation of authority related to the characteristics of management control systems (Chenhall, 2003). Decentralization also gives more responsibility and control for managers in operations and requires greater information as well (Waterhouse and Tiessen, 1978). The finding from Hoque (2011) is supported by this study.

Research and empirical finding support the results of this study in line with contingency theory argument. Based on (Chenhall, 2003) and (Otley, 1980) states the contingency theory of management accounting that when organizations implement management accounting and control systems in accordance with organizational factors such as decentralization will have a better performance. It is intended that the company will respond quickly and make decision directly related to management accounting and control systems. This empirical evidence from this research is supported by Hoque (2011).

Research and empirical findings support the results of this study in line with the argumentation Contingency Theory. It state that companies act more effectively if they apply and use management accounting control systems in accordance with organizational situations and social environment (Chapman, 1997); (Chenhall, 2003); (Chenhall and Chapman, 2006); (Otley, 1980). From the finding of this study indicate that the higher changes in management accounting and control systems, the higher performance of the organization.

This finding do not support prior studies that have been done by Mia and Clarke (1999), Hoque (2011) and Govindarajan (1984) which states that there is a positive relationship between the intensity of competition with organizational performance. This finding of this study supports Khandwalla (1972). Khandwalla (1972) in the United States state that a negative relationship between firm profitability and the level of product, as well as the network of market competition.

5. CONCLUSION

The intensity of competition is an environmental factor that cannot be controlled. In the face of competition intensity manufacturing companies will usually do the delegation of authority in its operation and a tendency to make changes in management accounting and control systems. This is

done by companies to maintain or achieve a competitive advantage compared to its competitors. The results showed that the relationship between the intensity of competition with the delegation of authority, change management and accounting control systems showed positive results and significant. On the relationship between the delegation of authority and organizational performance, and the relationship between changes in management accounting control systems and organizational performance showed significant results.

The limitation of this study is in the fit test models show result in marginal. Limitations on the level of *square multiple correlation* (R^2), which indicates the ability to explain of the variables is still relatively low, which means there are other variables that have the potential to be further investigated. Therefore the suggestion of future research needs to consider other variables to be studied as an example of information technology and organizational variables such as culture.

References

- Abdel-Kader, M., and R. Luther. 2008. The impact of firm characteristics on management accounting practices: A UK-based empirical analysis. *The British Accounting Review* 40 (1):2-27.
- Abernethy, and Bouwens. 2005. Determinants of accounting innovation implementation. *Abacus* 41 (3):217-240.
- Abernethy, and Stoelwinder. 1991. Budget use, task uncertainty, system goal orientation and sub unit performance: a test of 'fit' hypothesis in no-for-profit hospitals. *Accounting, Organizations and Society* 16:105-120.
- Ajibolade. 2013. Management accounting systems design and company performance in Nigerian manufacturing companies: A contingency theory perspective. *British Journal of Arts and Social Sciences* 14 (2):228-244.
- Ajibolade, S. Arowomole, and R. Ojikutu. 2010. Management accounting systems, perceived environmental Uncertainty and Companies' Performance in Nigeria. *International Journal of Academic Research* 2 (1):195-201.
- Chapman. 1997. Reflections on a contingent view of accounting. *Accounting, Organizations dan Society*. *Accounting, Organizations and Society* 22 (2):189-205.
- Chenhall. 2003. Management control systems design within its organizational context: findings from contingency-based research and directions for future. *Accounting, Organizations and Society* 28:127-168.
- . 2008. Accounting for the horizontal organization: A review essay. *Accounting, Organizations and Society* 33 517–550.
- Chenhall, R., and K. Langfield-Smith. 1998. The relationship between strategic priorities, management techniques dan management accounting: An empirical investigation using a systems approach. *Accounting, Organizations and Society* 23 (3):243-264.
- Danersen. 2001. Information technology, strategic decision making approaches dan organizational performance in different industrial settings *Journal of Strategic Information System* 10:101-119.
- Ezzamel. 1990. The impact of environmental uncertainty, managerial autonomy and size on budget characteristics. *Management Accounting Research* 1:181-197.
- Galbraith. 1977. *Organization Design*. United Kingdom: Addison Wesley.
- Ghozali. 2011. Konsep dan Penggunaan dengan Program AMOS 19. Semarang: Badan Penerbit Universitas Diponegoro.

- Gordon, and D. Miller. 1976. A contingency framework for the design of accounting information systems. *Accounting, Organizations, and Society* 1:59-69.
- Govindarajan. 1984. Appropriateness of accounting data in performance evaluations: An empirical examination of environmental uncertainty as an intervening variable. *Accounting, Organizations and Society* 9 (2):125-135.
- Govindarajan, and J. Fisher. 1990. Strategy, control systems, dan resource sharing: Effects on business-unit performance. *Academy of Management Journal*, 33 (2):259-285.
- Gul, F. A., and Y. Chia. 1994. The Effect of Management Accounting Systems, Perceived Environmental Uncertainty and Decentralization on Managerial Performance: A Test of Three Way Interaction *Accounting, Organizations and Society* 19 (5):413-426.
- Haldma, T., and K. Lääts. 2002. Contingencies influencing the management accounting practices of Estonian manufacturing companies. *Management Accounting Research* 13 (4):379-400.
- Hammad, S. A., R. Jusoh, and Ghozali. 2013. Decentralization, perceived environmental uncertainty, managerial performance and management accounting system information in Egyptian hospitals. *International Journal of Accounting and Information Management* 21 (4):314-330.
- Hoque, and W. James. 2000. Linking size and market factors to balanced scorecards: Impact on organizational performance. *Journal of Management Accounting Research* 12:1-17.
- Hoque, Z. 2011. The relations among competition, delegation, management accounting systems change and performance: A path model. *Advances in Accounting* 27 (2):266-277.
- Hoque, Z., L. Mia, and M. Alam. 2001. Market Competition, Computer-Aided Manufacturing and Use of Multiple Performance Measures: An Empirical Study. *The British Accounting Review* 33 (1):23-45.
- Isa. 2007. A Note on market competition, advanced manufacturing technology and management accounting and control systems change. *Malaysian Accounting Review* 6 (2):43-62.
- . 2009. Management Accounting Change Among Local and Foreign manufacturing Firms in Malaysia. *World Journal of Management* 1 (1):1-12.
- Isa, Foong, and Sambasivan. 2005. Roles of market competition and advanced manufacturing technology in predicting management accounting and control systems Change. *Asia Pacific Management Review* 10 (6):397-403.
- Ismail, and Isa. 2011. The Role of Management Accounting Systems In Advanced Manufacturing Environment. *Australian Journal of Basic and Applied Sciences* 5 (9):2196-2209.
- Kaplan, and A. A. Atkinson. 1998. *Advanced management accounting (3rd edition)*. Upper Saddle River, New Jersey: Prentice Hall.
- Khandwalla. 1972. The effects of different types of competition on the use of management controls. *Journal of Accounting Research* 10:275-285.
- Krishnan. 2005. The effect of changes in regulation and competition on firms' demand for accounting information. *The Accounting Review* 80 (1):269-287.

- Krishnan, J. Luft, and M. D. Shields. 2002. Competition and cost accounting: Adapting to changing markets. *Contemporary Accounting Research* 19:271-302.
- Lau, C. M., and M. Sholihin. 2005. Financial and nonfinancial performance measures: How do they affect job satisfaction? *The British Accounting Review* 37 (4):389-413.
- Lawrence, and Lorsch. 1967. *Organization dan environment*. Boston: Harvard Business School.
- Libby, and Waterhouse. 1996. Predicting Change in Management Accounting Systems. *Journal of Management Accounting Research* 8:137-150.
- Macy, and Arunachalam. 1995. Management Accounting Systems and Contingency Theory: in search of Effective Systems. *Advances in Management Accounting* 4:63-86.
- Manfield, R., and K. Alam. 1985. Decentralisation, Management Development and Organisational Performance in a Developing Country. *Personnel Review* (14):3.
- Mia, L. 1993. The Role of Management Accounting Systems Information in Organizations: An Empirical Study. *British Accounting Review* 25:269-285.
- Mia, L., and R. Chenhall. 1994. The usefulness of management accounting systems, functional differentiation dan managerial effectiveness *Accounting, Organizations and Society* 19 (1):1-13.
- Mia, L., and B. Clarke. 1999. Market competition, management accounting systems and business unit performance. *Management Accounting Research* 10 (2):137-158.
- Miah, and L. Mia. 1996. Decentralization, accounting controls dan performance of government organizations: A New Zealandan Empirical Study. *Financial Accountability dan Management* 12 (3):173-190.
- Mohamed, F. A. 2013. Changes in the business environment and the level of management accounting practices in Egypt: a case study. *Journal of American Science* 9 (10):78-89.
- Otley, D. 1980. The contingency theory of management accounting achievement and prognosis. *Accounting, Organizations and Society* 5 (4):413-428.
- Soobaroyen, and Poorundersing. 2008. The effectiveness of management accounting systems: Evidence from functional managers in a developing country. *Managerial Auditing Journal* 23 (2):187-219.
- Sulaiman, S., and F. Mitchell. 2005. Utilising a typology of management accounting change: An empirical analysis. *Management Accounting Research* 16 (4):422-437.
- Tuanmat, T. Z., D. Smith, and H. Djajadikerta. 2010. Determinants of Management Accounting Control Systems in Malaysian Manufacturing Firms. *Asian Journal of Accounting and Governance* 1:79-104.
- Verbeeten, F. H. 2010. The Impact of Business Unit Strategy, Structure dan Technical Innovativeness on Change in Management Accounting dan Control Systems at Business Unit Level: An Empirical Analysis. *International Journal of Management* 27 (1):123-143.
- Waterhouse, and Tiessen. 1978. A Contingency Framework for Management Accounting Systems Research. *Accounting, Organizations and Society* 3 (1):65-76.
- Waweru, Hoque, and Uliana. 2004. Management accounting change in South Africa Case studies from retail services. *Accounting, Auditing and Accountability Journal* 17 (5):675-704.

- Waweru, and Uliana. 2008. Predicting Change in management accounting systems: A contingent Approach. *Problems and Perspectives in Management* 6 (2):108-121.
- Williams, J. J., and A. E. Seaman. 2001. Predicting change in management accounting systems: national culture and industry effects. *Accounting, Organizations and Society* 26:443-460.
- . 2002. Management accounting systems change and departmental performance: the influence of managerial information and task uncertainty. *Management Accounting Research* 13 (4):419-445.

Hubungan Di Antara Keadilan, Kepercayaan Dengan Pematuhan Cukai Individu Di Malaysia

SELYWATI MOHD FAIZAL

Jabatan Perakaunan dan Kewangan
 Fakulti Perniagaan dan Perakaunan
 Infrastructure University of Kuala Lumpur
 Corporate Block, Unipark Suria, Jalan Ikram-Uniten, 43000 Kajang, Selangor
 MALAYSIA
 sellywati@iukl.edu.my

DR. MOHD RIZAL PALIL

Jabatan Perakaunan
 Fakulti Ekonomi dan Pengurusan
 Universiti Kebangsaan Malaysia
 43650 Bangi, Selangor
 MALAYSIA
 mr_palil@ukm.my

PROF. MADYA DR. RUHANITA MAELAH

Jabatan Perakaunan
 Fakulti Ekonomi dan Pengurusan
 Universiti Kebangsaan Malaysia
 43650 Bangi, Selangor
 MALAYSIA
 ruhanita@ukm.my

DR. ROSIATI RAMLI

Jabatan Perakaunan
 Fakulti Ekonomi dan Pengurusan
 Universiti Kebangsaan Malaysia
 43650 Bangi, Selangor
 MALAYSIA
 rosie@ukm.my

Abstrak

Kajian ini bertujuan untuk melihat hubungan di antara keadilan, kepercayaan dengan pematuhan cukai di Malaysia. Kajian terdahulu mengakui bahawa tanggapan keadilan mempunyai kesan ke atas pematuhan cukai. Kajian ini membezakan keadilan kepada keadilan prosedur, keadilan distributif dan keadilan retributif. Oleh itu, kajian ini akan mengkaji kesan ketiga-tiga keadilan ke atas pematuhan cukai. Dalam pada itu, kepercayaan turut mempengaruhi gelagat pematuhan cukai dan mempunyai hubungan dengan keadilan. Kajian ini mendapatkan persepsi daripada pembayar cukai individu penggajian melalui soal selidik yang telah digunakan dalam kajian terdahulu. Hasil kajian awal

membuktikan hanya keadilan prosedur dan kepercayaan mempengaruhi pematuhan cukai malah keadilan prosedur turut mempunyai hubungan positif dan signifikan dengan kepercayaan. Kajian ini akan menyumbang kepada literatur percukaian dengan menyediakan pengetahuan dengan memperluaskan skop tentang keadilan di Malaysia.

Katakunci: keadilan, kepercayaan

PENGENALAN

Sistem percukaian di Malaysia yang kini mengamalkan Sistem Taksir Sendiri (STS) membenarkan pembayar cukai bertanggungjawab untuk menilai, menentukan dan membayar liabiliti cukai mereka sendiri mengikut undang-undang cukai. Ini bagi menggalakkan pembayar cukai untuk menjadi lebih jujur dan bertanggungjawab dalam pengiraan cukai mereka. Namun begitu, sesetengah pembayar cukai mungkin cuba mengambil kesempatan dengan memanipulasi urusan kewangan mereka agar membayar cukai kurang atau tidak perlu membayar langsung cukai (Murphy 2004).

Oleh itu, pelbagai usaha dan tindakan yang diambil oleh Lembaga Hasil Dalam Negeri (LHDN) sebagai pihak berkuasa cukai di Malaysia bagi membendung masalah ketidakpatuhan. Sebagai contoh, aktiviti penyiasatan terhadap kes berprofil tinggi dilaksanakan dalam usaha meningkatkan pematuhan yang terbahagi kepada Siasatan Sivil dan Siasatan Jenayah. Pada tahun 2010 penyelesaian bagi kes Siasatan Sivil adalah 961 kes dengan jumlah cukai dan penalti RM811.5 juta (LHDN 2011). Manakala, bagi Siasatan Jenayah pula sepanjang tahun 2010, sebanyak 10 kertas siasatan telah diselesaikan manakala 30 kes lagi masih dalam siasatan yang mungkin membawa kepada tindakan pendakwaan di mahkamah (LHDN 2011).

Seterusnya, penguatkuasaan bagi larangan meninggalkan negara (Seksyen 104, Akta Cukai Pendapatan 1967) diambil ke atas pembayar cukai yang gagal menjelaskan tanggungan cukai pendapatan serta dipercayai akan keluar atau meninggalkan negara. Seramai 72,013 pembayar cukai bagi kategori cukai pendapatan telah dikenakan tindakan larangan tersebut pada 2011 yang melibatkan jumlah tunggakan cukai sebanyak RM218.12 juta.

Statistik-statistik tersebut secara tidak langsung menunjukkan wujud tindakan ketidakpatuhan cukai di kalangan pembayar cukai di Malaysia walaupun tindakan tegas diambil oleh pihak berkuasa cukai di Malaysia. Ketidakpatuhan cukai yang berlaku mungkin disebabkan persepsi keadilan yang mempengaruhi tindakan mereka (Natrah 2009). Terutamanya apabila pembayar cukai berpendapat bahawa pembayar cukai yang berada dalam kedudukan ekonomi atau pendapatan yang sama perlu dikenakan cukai pada kadar yang sama (Gravelle & Gravelle 2006). Dalam erti kata lain, pembayar cukai yang mempunyai pendapatan, kekayaan serta tanggungan yang sama perlulah dicukai pada kadar yang sama.

Keadilan juga merupakan antara salah satu daripada empat ciri yang perlu ada dalam sistem percukaian yang dibincangkan oleh Adam Smith pada tahun 1776 (Lymer & Oats 2009). Prinsip keadilan menekankan bahawa individu mesti dikenakan cukai berdasarkan kemampuan mereka yang dibahagikan kepada keadilan melintang dan keadilan menegak. Keadilan melintang ialah apabila individu yang mempunyai pendapatan yang sama perlu dikenakan cukai pada kadar yang sama atau menanggung beban cukai yang sama. Manakala, keadilan menegak ialah membezakan di antara individu yang mempunyai kedudukan pendapatan yang berbeza (Barjoyai 1987).

Disebabkan itu, tanggapan keadilan dalam sistem percukaian dilihat berperanan dalam mempengaruhi tahap pematuhan di kalangan pembayar cukai. Beberapa kajian mendapati pembayar cukai lebih cenderung untuk patuh apabila sistem percukaian sesebuah Negara dianggap adil dan saksama (seperti Alm et al. 1993; Richardson 2005; Gilligan & Richardson 2005; Anna & Perumal 2008).

Kajian ini berbeza dengan kajian-kajian keadilan yang telah dijalankan. Pertama, kajian-kajian yang pernah dijalankan menggunakan pelbagai dimensi dan analisis faktor bagi mengukur tanggapan keadilan seperti keadilan menegak, keadilan melintang, keadilan pertukaran, keadilan pentadbiran, dan lain-lain. Menurut Wenzel (2002a), hasil daripada analisis faktor bergantung kepada ukuran yang sesuai dengan analisis di mana konsep dimensi tidak boleh diputuskan dalam kajian secara empirikal. Oleh itu, beliau memperkenalkan kerangka kerja keadilan sebagai panduan pengukuran secara sistematik dalam mengkaji peranan keadilan ke atas sikap dan gelagat pembayar cukai. Wenzel (2002a) membahagikan keadilan kepada tiga iaitu keadilan prosedur, keadilan distributif dan keadilan retributif yang biasanya digunakan dalam bidang sosial psikologi. Oleh itu, kajian ini akan melihat hubungan ketiga-tiga keadilan dengan pematuhan cukai. Beberapa kajian mendapati wujud hubungan di antara ketiga-tiga keadilan dengan pematuhan cukai.

Kedua, kajian ini juga berbeza daripada kajian keadilan yang telah kajian telah dijalankan di Malaysia oleh Anna dan Perumal (2008); Natrah (2009) dan Natrah (2012). Kajian oleh Anna dan Perumal (2008) membuktikan tanggapan keadilan yang diadaptasi daripada dimensi keadilan yang digunakan oleh Gebing (1988) wujud di Malaysia. Walau bagaimanapun, kajian yang dijalankan tidak mengkaji kesan tanggapan keadilan tersebut ke atas pematuhan cukai. Manakala, Natrah (2009) dan Natrah (2012) pula mengkaji peranan tanggapan keadilan ke atas pematuhan cukai dan melihat kesan pengetahuan cukai dan kompleksiti cukai ke atas keadilan. Hasil kajian oleh Natrah (2009) mendapati pembayar cukai mempunyai tanggapan bahawa sistem percukaian semasa adalah adil, namun tiada bukti yang menunjukkan tanggapan tersebut mempengaruhi gelagat pematuhan. Hasil yang sama juga diperolehi oleh Natrah (2012) yang melihat tanggapan keadilan di kalangan pembayar cukai di Malaysia dan New Zealand. Pembayar cukai di Malaysia mempunyai persepsi keadilan lebih positif dan signifikan tentang sistem percukaian di Malaysia berbanding pembayar cukai di New Zealand. Namun demikian, pembayar cukai di New Zealand lebih patuh dan menjalankan tanggungjawab cukai mereka berbanding pembayar cukai di Malaysia.

Ketiga, kajian ini juga akan melihat hubungan ketiga-tiga keadilan dengan kepercayaan terhadap pihak berkuasa cukai dan hubungan kepercayaan dengan pematuhan cukai. Ini kerana, kepercayaan juga dianggap sebagai indikator bagi menilai tahap keadilan prosedur pihak berkuasa (Konovsky & Pugh 1994). Dalam kajian yang lain pula, kepercayaan dilihat mampu mempengaruhi pematuhan cukai. Sebagai contoh, kajian yang dijalankan oleh Wahl et al. (2010) dan Kastlunger et al. (2013) mendapati kepercayaan terhadap pihak berkuasa cukai yang tinggi mampu meningkatkan pematuhan cukai. Kirchler (2007) mengklasifikasikan kepercayaan sebagai faktor yang mempunyai hubungan positif dan signifikan bagi meningkatkan tahap pematuhan cukai. Tambahan itu, kajian ini juga akan menentukan hubungan di antara keadilan distributif dan keadilan retributif dengan kepercayaan yang masih belum pernah dikaji. Kajian ini akan mengkaji kesan faktor-faktor tersebut ke atas pematuhan cukai.

Kini, belum ada kajian menyeluruh dijalankan bagi mengenalpasti hubungan di antara tanggapan keadilan prosedur, keadilan distributif dan keadilan retributif dengan pematuhan cukai di Malaysia. Maka, kajian ini berusaha untuk mengatasi jurang tersebut. Oleh yang demikian, objektif utama kajian ini ialah untuk menentukan hubungan di antara tanggapan keadilan yang terdiri daripada keadilan prosedur, keadilan distributif dan keadilan retributif serta kepercayaan dengan gelagat pematuhan

cukai di Malaysia. Tambahan itu, kajian ini akan melihat hubungan di antara ketiga-tiga keadilan dengan kepercayaan.

Kajian ini disusun seperti berikut dengan kajian terdahulu berkaitan pembolehubah-pembolehubah kajian yang terlibat yang seterusnya membentuk hipotesis dibincangkan dibahagian berikutnya. Kaedah kajian diterangkan di bahagian seterusnya. Hasil awalan kajian diperbincangkan diakhir bahagian kajian ini.

KAJIAN TERDAHULU DAN PEMBENTUKAN HIPOTESIS

Hubungan di antara keadilan dengan pematuhan cukai

Menurut Murphy dan Tyler (2008), jika layanan yang baik dan adil diterima oleh pembayar cukai daripada pihak berkuasa cukai, mereka akan memberikan kerjasama dan akan menjadi lebih patuh dengan keputusan yang dibuat oleh pihak berkuasa cukai. Wenzel (2002b) mendapati keadilan prosedur mampu meramal tahap pematuhan di kalangan pembayar cukai di Australia. Hasil kajian beliau menunjukkan bahawa pembayar cukai menjadi lebih patuh apabila mereka merasakan pegawai cukai melayan mereka secara adil dan penuh hormat. Keadilan prosedur merujuk kepada persepsi tentang layanan yang diterima oleh individu daripada pihak berkuasa (Murphy 2009) dan ianya juga berkaitan dengan proses pembahagian sumber oleh pihak berkuasa (Kirchler 2007).

Di dalam percubaian, kajian tentang keadilan prosedur yang telah dijalankan menunjukkan bahawa ianya mempunyai kesan positif terhadap pematuhan cukai. Terdapat kajian empirikal yang menunjukkan bahawa jika individu beranggapan bahawa pihak berkuasa menjalankan prosedur yang sedia ada secara adil, maka mereka akan lebih percaya kepada pihak berkuasa tersebut (Murphy 2004) malah akan lebih patuh dengan segala keputusan yang dibuat oleh pihak berkuasa cukai (Murphy & Tyler 2008).

Walau bagaimanapun, kajian-kajian terdahulu berkaitan keadilan prosedur tidak memperoleh keputusan yang konsisten. Terdapat pengkaji melaporkan keadilan prosedur mempunyai kesan positif (van Dijke & Verboon 2010), namun terdapat juga pengkaji yang gagal melihat kesan tersebut (Worsham 1996). Begitu juga dengan keadilan distributif yang turut mempengaruhi gelagat pematuhan cukai. Keadilan distributif merujuk kepada tanggapan sejauh mana input yang disumbangkan mampu memperolehi hasil yang sepatutnya bagi mencapai tahap kesaksamaan (Adams 1965; Walster et al. 1973).

Kebanyakan kajian membuktikan bahawa keadilan distributif mempunyai kesan ke atas pematuhan cukai. Pembayar cukai melakukan pelarian cukai apabila mereka merasakan wujud ketidakadilan dalam hubungan pertukaran di antara pembayar cukai dengan kerajaan (Porcano 1984; Kim 2002; Verboon & van Dijke 2007). Pembayar cukai yang tidak menerima pertukaran awam daripada kerajaan merasakan bahawa berlakunya ketidakadilan berbanding mereka yang menerima pertukaran awam. Keadaan sama juga berlaku apabila pembayar cukai tidak bersetuju dengan polisi perbelanjaan kerajaan atau berpendapat bahawa mereka tidak menerima pertukaran yang adil daripada kerajaan, mereka akan merasa tertekan dan seterusnya akan melakukan ketidakpatuhan cukai (Kim 2002).

Moser et al. (1995) dalam kajian mereka membuktikan bahawa ketidakpatuhan cukai berlaku apabila responden dikenakan kadar cukai tinggi berbanding pembayar cukai lain dan menerima barangan

awam yang setimpal dengan bayaran cukai mereka. Semakin tinggi hasil yang diterima daripada bayaran cukai, maka semakin tinggi tahap pematuhan cukai (Alm et al. 1992a; Alm et al. 1992b).

Walaupun tidak banyak kajian yang dijalankan bagi melihat hubungan di antara keadilan retributif dengan pematuhan cukai, namun kajian yang telah dijalankan membuktikan wujud hubungan di antara kedua-dua pembolehubah. Keadilan retributif merujuk kepada tanggapan tentang hukuman yang sesuai apabila berlakunya pelanggaran norma. Ianya merangkumi peruntukkan tanggungjawab ke atas mereka yang bersalah melakukan kesalahan dengan mengenakan hukuman setimpal terhadap kesalahan yang dilakukan (Kirchler 2007). Dalam percukaian pelbagai hukuman dikenakan ke atas ketidakpatuhan cukai, maka hukuman yang dikenakan mestilah sesuai dengan kesalahan yang dilakukan (Natrah 2011).

Apabila pembayar cukai merasakan terdapatnya keadilan dalam sistem percukaian yang dikenakan ke atas pesalah cukai maka pematuhan cukai turut meningkat (Natrah 2011). Selain daripada hukuman, ganjaran yang diberikan kepada pembayar cukai yang patuh turut mempengaruhi gelagat pematuhan (Falkinger & Walther 1991). Justeru itu, hipotesis berikut dibentuk bagi melihat hubungan di antara ketiga-tiga jenis keadilan dengan pematuhan cukai sama ada secara sukarela mahupun secara kuatkuasa. Berdasarkan perbincangan, hipotesis seperti di bawah dibentuk:

H1a: Keadilan prosedur mempunyai hubungan positif dengan pematuhan cukai.

H1b: Keadilan distributif mempunyai hubungan positif dengan pematuhan cukai.

H1c: Keadilan retributif mempunyai hubungan positif dengan pematuhan cukai.

Hubungan di antara kepercayaan dengan pematuhan cukai

Kepercayaan memberi penekanan tentang hubungan di antara pembayar cukai dan pihak berkuasa cukai hasil daripada rasa percaya pembayar cukai terhadap pihak berkuasa cukai dalam menjalankan aktiviti percukaian. Jika pembayar cukai mempunyai tahap kepercayaan yang tinggi terhadap pihak berkuasa cukai maka pematuhan juga meningkat (Kastlunger et al. 2013).

Wahl et al. (2010) dalam kajian mereka untuk melihat kesan kuasa dan kepercayaan ke atas pembayaran cukai menemukan kesan positif kuasa dan kepercayaan ke atas pembayaran cukai. Tahap kepercayaan yang tinggi pihak berkuasa mampu meningkatkan tahap pematuhan cukai sama ada secara sukarela mahupun secara kuatkuasa. Begitu juga kajian yang dijalankan oleh Muehlbacher et al. (2011) dan Kogler et al. (2013) mendapati kepercayaan terhadap pihak berkuasa cukai meningkatkan pematuhan sukarela. Maka, hipotesis berikut dibentuk:

H2: Kepercayaan mempunyai hubungan positif dengan pematuhan cukai.

Hubungan di antara keadilan dengan kepercayaan

Keadilan prosedur dan kepercayaan terhadap pihak berkuasa mampu menerangkan hubungan di antara pihak berkuasa dan rakyat (De Cremer & Tyler 2007). Jika individu beranggapan pihak berkuasa menjalankan prosedur yang sedia ada secara adil, maka mereka akan lebih percaya kepada pihak berkuasa tersebut (Murphy 2004). Di dalam bidang percukaian, hubungan di antara pembayar cukai dan pihak berkuasa cukai wujud apabila saling mempercayai dan berkerjasama diperlukan bagi mencapai pematuhan cukai. Layanan adil yang diterima oleh pembayar cukai akan meningkatkan keyakinan dan kepercayaan terhadap pihak berkuasa cukai. Keadaan ini mampu membantu pihak berkuasa cukai mencapai pematuhan cukai yang tinggi.

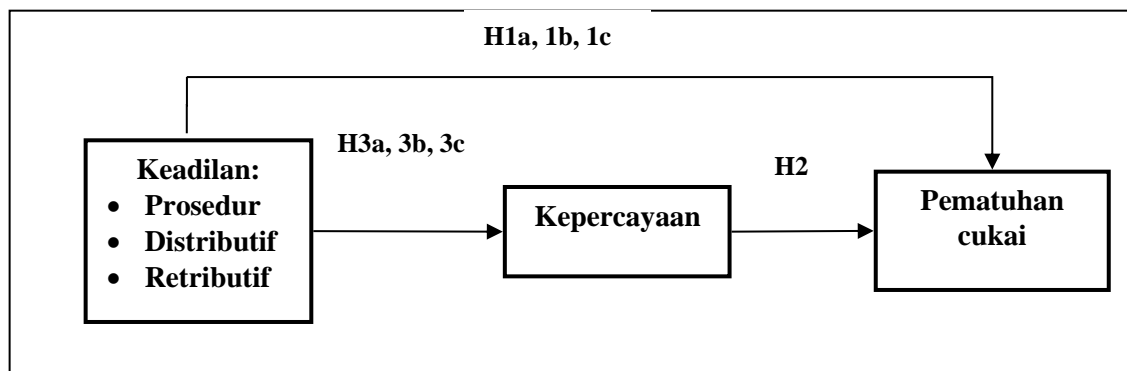
Di Australia, tahap kepercayaan terhadap pihak berkuasa cukai pada tahap rendah disebabkan layanan tidak adil diterima oleh mereka (Murphy 2004). Jelaslah bahawa, wujud hubungan di antara layanan secara adil yang diterima oleh pembayar cukai dan kepercayaan terhadap pihak berkuasa cukai. Selain itu, kajian ini juga akan melihat hubungan di antara keadilan distributif dan keadilan retributif dengan kepercayaan tersebut melalui pembentukan hipotesis berikut:

H3a: Keadilan prosedur mempunyai hubungan positif dengan kepercayaan.

H3b: Keadilan distributif mempunyai hubungan positif dengan kepercayaan.

H3c: Keadilan retributif mempunyai hubungan positif dengan kepercayaan.

Rajah 1 berikut adalah kerangka kerja kajian:



RAJAH 1: Kerangka kerja kajian

KAEDAH KAJIAN

Kajian ini menggunakan pendekatan kuantitatif bagi mendapatkan pendapat responden tentang keadilan dalam sistem percukaian di Malaysia. Kajian ini memperolehi maklumat melalui kerja lapangan dengan menggunakan soal selidik. Data awal kajian ini diperolehi daripada pembayar cukai individu yang terdiri daripada penggajian. Soalan yang terdapat di dalam soal selidik diadaptasi daripada kajian terdahulu tentang kepercayaan dan pematuhan cukai yang telah dijalankan oleh Kirchler dan Wahl (2010) dan Kustlunger et al. (2013), keadilan prosedur yang diadaptasi oleh Murphy (2009) yang dibangunkan oleh Tyler (2006), keadilan distributif diperolehi daripada Verboon dan van Dijke (2007) serta keadilan retributif diambil daripada kajian yang dijalankan oleh Natrah (2011). Soalan diubah mengikut kesesuaian keadaan di Malaysia. Soal selidik dwi bahasa direka bagi memudahkan responden memahami soalan yang diajukan.

Soal selidik yang digunakan dalam kajian ini mengandungi pernyataan-pernyataan untuk mengukur setiap pembolehubah. Pengukuran terhadap pembolehubah ialah dengan melihat persepsi responden tentang pematuhan cukai sukarela, pematuhan cukai secara kuatkuasa, kepercayaan, kuasa legitimasi, kuasa paksaan, keadilan prosedur, keadilan distributif dan keadilan retributif. Persepsi responden diukur dengan menggunakan skala Likert untuk menentukan tahap persetujuan terhadap pernyataan yang diberikan (skala Likert 5 mata, 1 = sangat tidak setuju, 2 = tidak bersetuju, 3 = tidak pasti, 4 = setuju dan 5 = sangat setuju).

HASIL AWALAN KAJIAN DAN PERBINCANGAN

41 soal selidik diberikan kepada responden yang terdiri ahli akademik, pengamal industri, kakitangan kerajaan dan bukan kerajaan. Walau bagaimanapun, hanya 40 soal selidik yang boleh diguna pakai



bagi tujuan analisis data. Daripada jumlah tersebut 14 orang (35%) responden adalah lelaki dan 26 orang (65%) pula perempuan dengan kakitangan kerajaan seramai 13 orang (32.5%) dan selebihnya 27 orang (67.5%) terdiri daripada bukan kakitangan kerajaan. Seterusnya, daripada keseluruhan reponden yang terlibat seramai 38 orang mempunyai pendapatan bulanan melebihi RM2,700 dengan pecahan pendapatan RM2,701-RM4,000 (19 orang), RM4,001-RM6,000 (15 orang), RM6,001-RM8,000 (3 orang) dan RM8,001-RM10,000 (seorang). Hanya 2 orang (5%) reponden yang mempunyai pendapatan bulanan kurang daripada RM2,001.

Ujian korelasi

Kajian ini menggunakan ujian korelasi bagi melihat hubungan di antara pembolehubah-pembolehubah kajian. Hasil analisis menunjukkan keadilan dan kepercayaan berhubung kait dengan pematuhan cukai individu dengan mempunyai hubungan yang positif dan signifikan iaitu (keadilan = 0.428 dan kepercayaan = 0.435). Sementara itu, keputusan bagi hubungan ketiga-tiga jenis keadilan dengan pematuhan cukai pembayar cukai menunjukkan keputusan berbeza-beza. Keadilan prosedur dan keadilan retributif mempunyai hubungan positif dengan pematuhan cukai (keadilan prosedur = 0.398 dan keadilan retributif = 0.214) manakala keadilan distributif mempunyai hubungan negatif dengan skor -0.071. Namun hanya keadilan prosedur mempunyai hubungan yang signifikan pematuhan cukai di Malaysia.

Tambahan itu, bagi hubungan di antara keadilan dan kepercayaan secara keseluruhan menunjukkan hubungan positif yang signifikan (0.0682). Sementara itu, apabila keadilan dibahagikan hanya keadilan retributif mempunyai hubungan tidak signifikan dengan kepercayaan. Manakala, keadilan prosedur mampu mempengaruhi tahap kepercayaan terhadap pihak berkuasa cukai (0.820), namun tidak bagi keadilan distributif yang menunjukkan ianya mempunyai hubungan negatif dan signifikan dengan kepercayaan (-0.329). Jadual 1 menunjukkan korelasi bagi hubungan di antara pembolehubah-pembolehubah.

JADUAL 1: Korelasi Pearson

	Pematuhan	Keadilan Prosedur	Keadilan Distributif	Keadilan retributif	Keadilan	Percaya
Pematuhan	1.00	.398 (.011)*	-.071 (.662)	.214 (.185)	.428 (.006)**	.435 (.005)**
Keadilan Prosedur		1.00	-.344 (.030)*	.044 (.788)	.848 (.000)**	.820 (.000)**
Keadilan Distributif			1.00	.288 (.072)	.095 (.561)	-.329 (.038)*
Keadilan Retributif				1.00	.486 (.001)**	.042 (.795)
Keadilan					1.00	.682 (.000)**
Percaya						1.00

*signifikan pada 0.05 dengan 2-tailed

**signifikan pada 0.01 dengan 2-tailed

Ternyata hasil ujian ini menyokong hipotesis 1a dan hipotesis 2 yang menjangkakan keadilan prosedur dan kepercayaan mempunyai hubungan positif dengan pematuhan cukai. Begitu juga dengan hipotesis 3a. Ini bermakna apabila pembayar cukai merasakan bahawa mereka menerima layanan yang baik dan mempunyai rasa percaya yang tinggi terhadap pihak berkuasa cukai, tanggapan ini mendorong mereka untuk lebih patuh. Layanan yang baik juga turut mempengaruhi tahap kepercayaan pembayar cukai terhadap pihak berkuasa cukai. Bagi hipotesis 1b, 1c, 3b dan 3c pula menjangkakan keadilan distributif dan keadilan retributif mempunyai hubungan positif dengan pematuhan cukai serta kepercayaan. Walau bagaimanapun hasil ujian mendapati keempat-empat hipotesis tersebut ditolak. Keadilan distributif dilihat mempunyai hubungan negatif dengan pematuhan cukai dan kepercayaan, manakala keadilan retributif mempunyai hubungan positif tetapi tidak signifikan dengan pematuhan cukai dan kepercayaan. Namun begitu, apabila ketiga-tiga keadilan disatukan hasil menunjukkan keadilan mampu mempengaruhi pematuhan cukai dan juga kepercayaan.

RUMUSAN

Persepsi tentang keadilan sistem percukaian dan kepercayaan terhadap pihak berkuasa cukai mampu meningkatkan tahap pematuhan cukai. Walau bagaimanapun, kajian ini masih diperingkat permulaan dengan hasil analisis awalan yang dijalankan menunjukkan tidak menyokong beberapa hipotesis.

Senarai rujukan:

- Adams, J. (1965). Inequity in social change. *Advances in Experimental Social Psychology*, 2, 267-299.
- Alm, J., McClelland, G.H., & Schulze, W.D. (1992a). Why people pay taxes?. *Journal of Public Economics*, 48, 21-38.
- Alm, J., Jackson, B.R., & Mckee, M. (1992b). Estimating the determinants of taxpayer compliance with experimental data. *National Tax Journal*, 45(1), 107-114.
- Alm, J., Cronshaw, M.B., & McKnee, M. (1993). Tax compliance with endogenous audit selection. *Kyklos*, 46(1), 27-45.
- Anna A. Che Azmi & Kamala A. Perumal. (2008). Tax fairness dimensions in Asian Context: the Malaysian perspective. *International Review of Business Research Papers*, 4(5), 11-19.
- Barjoiyai, B. (1987). *Taxation: Principle and Practice in Malaysia (Pencukaian Prinsip dan Amalan di Malaysia)*. Kuala Lumpur: Dewan Bahasa dan Pustaka.
- De Cremer., D & Tyler., T.R. (2007). The effect of trust in authority and procedural fairness on cooperation. *Journal of Applied Psychology*, 92(3), 639-649.
- Falkinger., J & Walther., H. (1991). Rewards versus penalties: on a new policy against tax evasion. *Public Finance Review*, 19(1), 67-79.

- Gerbing, M.D. (1988). 'An empirical study of taxpayer perceptions of fairness'. Unpublished PhD Thesis, University of Texas in Anna A. Che Azmi & Kamala A. Perumal. (2008). Tax fairness dimensions in Asian Context: the Malaysian perspective. *International Review of Business Research Papers*, 4(5), 11-19.
- Gilligan, G., & Richardson, G. (2005). Perceptions of tax fairness and tax compliance in Australia and Hong Kong – A Preliminary Study. *Journal of Financial Crime*, 12(4), 31-342.
- Gravelle, J., & Gravelle, J. (2006). Horizontal equity and family tax treatment: The orphan child of tax policy. *National Tax Journal*, 59(3), 631-649.
- Kastlunger, B., Lozza, E., Kirchler, E., & Schabmann, A. (2013). Powerful authorities and trusting citizens: the slippery slope framework and tax compliance in Italy. *Journal of Economic Psychology*, 34, 36-45.
- Kim., C.K. (2002). Does fairness matter in tax reporting behavior?. *Journal of Economic Psychology*, 23, 771-785.
- Kirchler, E. (2007). *The economic psychology of tax behaviour*. United Kingdom: Cambridge University Press.
- Kirchler, E., & Wahl, I. (2010). Tax compliance inventory TAX-I: Designing an inventory for surveys of tax compliance. *Journal of Economic Psychology*, 31, 331-346.
- Kogler, C., Batrancea, L., Nichita, A., Pantya, J., Belianin, A., & Kirchler, E. (2013). Trust and power as determinants of tax compliance: testing the assumptions of the slippery slope framework in Austria, Hungary, Romania and Russia. *Journal of Economic Psychology*, 34(2013), 169-180.
- Konovsky, M. A., & Pugh, S.D. (1994). Citizenship behavior and social exchange. *Academic of Management Journal*, 37(3), 656-669.
- Lembaga Hasil Dalam Negeri. (2011). *Laporan Tahunan LHDN*.
- Lymer, A., and Oats, L. (2009). *Taxation: Policy and Practice*. 16th ed. Birmingham: Fiscal Publications.
- Moser, D.V., Evans III, J.H., & Kim, C.K. (1995). The effects of horizontal and exchange inequity on tax reporting decisions. *The Accounting Review*, 70(4), 619-634.
- Muehlbacher, S., Kirchler, E., & Schwarzenberger, H. (2011). Voluntary versus enforced tax compliance: empirical evidence for the "slippery slope" framework. *European Journal of Law Economic*, 32, 89-97.
- Murphy, K. (2004). The role of trust in nurturing compliance: a study of accused tax avoiders. *Law and human Behavior*, 28(2), 187-209.

- Murphy, K. (2009). Procedural justice and affect intensity: understanding reactions to regulatory authorities. *Social Justice Research*, 22, 1-30.
- Murphy, K., & Tyler, T. (2008). Procedural justice and compliance behaviour: the mediating role of emotions. *European Journal of Social Psychology*, 38(4), 652-668.
- Natrah, S. (2009). Fairness perceptions and compliance behaviour: the case of salaried taxpayers in Malaysia after implementation of the self-assessment system. *e-Journal Tax Research*, 8(1), 32-63.
- Natrah, S. (2011). *Fairness perceptions and compliance behavior: taxpayers' judgements in self-assessment environments*. Unpublished doctoral thesis, University of Canterbury, Australia.
- Natrah, S. (2012). Perceptions of tax fairness and tax compliance behaviour: a comparative study. *Jurnal Pengurusan*, 36, 89-100.
- Porcano, T.M. (1984). Distributive Justice and Tax Policy. *The Accounting Review*, 59: 619-36.
- Richardson, G. (2005). An exploratory cross-cultural study of tax fairness perceptions and tax compliance behavior in Australia and Hong Kong. *International Tax Journal*, winter, 11-67.
- Tyler, T. R. (2006). Why people obey the law. New Haven, CT: Yale University Press.
- Kastlunger, B., Lozza, E., Kirchler, E., & Schabmann, A. (2013). Powerful authorities and trusting citizens: the slippery slope framework and tax compliance in Italy. *Journal of Economic Psychology*, 34, 36-45.
- Wahl, I., Kastlunger, B., & Kirchler, E. (2010). Trust in authorities and power to enforce tax compliance: an empirical analysis of the 'slippery slope framework'. *Law & Policy*, 32(4), 383-406.
- Walster, E., Walster, G., Berscheid, E. (1973). New directions in equity research. *Journal of Personality and Social Psychology*, 25(2), 151-176.
- Wenzel, M. (2002a). Tax compliance and the psychology of justice: mapping the field. In: Taxing democracy. Braithwaite, V. (ed.) Farnham, Ashgate, 41-69.
- Wenzel, M. (2002b). The impact of outcome orientation and justice concerns on tax compliance: the role of taxpayers' identity. *Journal of Applied Psychology*, 87: 629-645.
- Worsham, R.G.J. (1996). The effect of tax authority behavior on taxpayer compliance a procedure justice approach. *Journal of the American Taxation Association*, 18(2), 19-39.
- van Dijke, M & Verboon, P. (2010). Trust in authorities as a boundary condition to procedural fairness effects on tax compliance. *Journal of Economic Psychology*, 31, 80-91.



Verboon, P., & van Dijke, M. (2007). A self-interest analysis of justice and tax compliance: how distributive justice moderates the effect of outcome favourability. *Journal of Economic Psychology*, 28, 704–727.

Alamat:

Jabatan Perakaunan dan Kewangan
Fakulti Perniagaan dan Perakaunan
Infrastructure University of Kuala Lumpur
Corporate Block, Unipark Suria, Jalan Ikram-Uniten, 43000 Kajang, Selangor
MALAYSIA

Jabatan Perakaunan
Fakulti Ekonomi dan Pengurusan
Universiti Kebangsaan Malaysia
43650 Bangi, Selangor
MALAYSIA