



UNIVERSITI PUTRA MALAYSIA

**THE MALAYSIAN CORPORATE GOVERNANCE REFORM AND
FINANCIAL REPORTING QUALITY**

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AND FINANCIAL REPORTING QUALITY**

By

HAIRUL SUHAIMI B. NAHAR

**Thesis Submitted to the Graduate School of Management,
Universiti Putra Malaysia, in Fulfillment of the
Requirement for the Degree of Doctor of Philosophy**

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DEDICATION

I dedicate this thesis to my beloved parents–Haji Nahar b. Maarop (Allahyarham: 4th February 2011) and Hajjah Asmah Hanam bt. Ahmad Marzuki (Allahyarham: 21st February 1993); parents-in-law–Haji Mustapha b. Mohamad and Hajjah Saniah bt. Isa; my beloved wife–Murnilawati; and our only daughter–Nur Arina.

Abstract of thesis presented to the Senate of Universiti Putra Malaysia in fulfillment of the requirement for the degree of Doctor of Philosophy

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Chains of critical corporate and economic events pre and post millennium periods have dramatically shifted the focus of firms, investors and regulators worldwide on corporate governance and financial reporting issues. Particularly, the 1997/1998 Asian financial crisis has motivated many Asian countries including Malaysia to reform their respective governance regime. This study undertakes an empirical investigation with regards to the Malaysian public policy reform effectiveness related to corporate governance from the specific perspective of firm's financial reporting quality (FRQ). The motivation behind this study is the propositions set out by the Malaysian government upon introducing series of governance reform programs which includes the expectation that reform programs would improve directors' monitoring and oversight effectiveness towards financial reporting matters. These propositions are considered in this study as "maintained assumptions", which become the subject of the empirical investigation.

Accordingly, three research objectives and three main hypotheses were established. Six board characteristics and two ownership types were selected, representing the predictor variables. Contributing to the body of governance knowledge is the consideration given to a new director's characteristic of social title which is Malaysia's unique board feature. Other board characteristics include leadership structure, independence, multiple directorships, founding family directors and financial expertise. The two considered ownership types are directors' and institutions' and the FRQ being the dependent variable is proxied by accruals quality metrics commonly used in prior FRQ studies. A total of one hundred and three survived listed firms in *Bursa* Malaysia throughout the eleven years period from 1996 to 2006, with complete data were chosen.

The survived firms were sampled to accommodate the balanced observations research design, thereby facilitating the objective assessment of governance reform implications on firm's FRQ. The regression analyses were done separately to reflect the two separate reform types of regulatory (reform-I) and institutional and best practices (reform-II). This thesis postulates that the introduction of both reform types would introduce an inflexion point to firm's FRQ (i.e. improvement) and favorably moderate the statistical relationships between firm's FRQ and both, board and ownership variables.

The results indicate that majority (88% in reform-I and 75% in reform-II analysis period) of the predictor variables considered in this study are significant determinants of FRQ (in the predicted direction) in Malaysia. The interaction results (testing on reforms' moderating effect) generally reflect poor ability of reform-I to favorably

moderate the link between predictor variables and FRQ as compared to reform-II, indirectly suggesting higher moderating effectiveness of reform-II. The study is however unable to find any evidence of FRQ improvement post reform periods. Three reasons of (1) the macroeconomic condition; (2) the importance of governance in enhancing firm's FRQ; and (3) the presence of unique, country-specific economic and governance characteristics are suggested to explain the findings. The sensitivity tests results suggest that, except for some minor differences in results, these findings are moderately robust to alternative variables specification and study period. Overall, this study contributes to the extant of governance literature in emerging economies by evidencing that governance reform effectiveness in ensuring firm's FRQ is sensitive to economic conditions and various unique governance and institutional characteristics.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia
sebagai memenuhi keperluan untuk Ijazah Doktor Falsafah

**REFORMASI URUS TADBIR KORPORAT DI MALAYSIA DAN KUALITI
PELAPORAN KEWANGAN**

Oleh

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Rantaian peristiwa korporat dan ekonomi yang berlaku sebelum dan selepas *milenium* telah mengubah fokus syarikat, pelabur dan penggubal undang-undang di seluruh dunia terhadap isu urus tadbir korporat dan pelaporan kewangan. Khususnya, peristiwa krisis kewangan Asia pada 1997/1998 telah memberi motivasi kepada negara-negara Asia termasuk Malaysia untuk mereformasi rejim urus tadbir korporat mereka masing-masing. Kajian ini membuat siasatan empirikal mengenai keberkesanan reformasi polisi awam berkaitan dengan urus tadbir korporat di Malaysia khususnya dari perspektif kualiti pelaporan kewangan (KPK). Kajian ini didorong oleh jangkaan yang dibuat oleh kerajaan Malaysia semasa melaksanakan program-program reformasi urus tadbir korporat, termasuklah jangkaan bahawa program-program reformasi tersebut akan menambah baik tahap pemantauan oleh pengarah syarikat terhadap perkara-perkara berkaitan pelaporan kewangan. Jangkaan ini dianggap sebagai andaian tetap yang menjadi subjek kepada siasatan empirikal di dalam kajian ini.

Jesteru, tiga objektif kajian dan tiga hipotesis utama telah dibina. Enam ciri-ciri lembaga pengarah dan dua jenis pemilikan telah dipilih, mewakili pemboleh ubah penentu. Menyumbang kepada ilmu urus tadbir korporat ialah pertimbangan yang diberikan kepada ciri baru pengarah iaitu pangkat sosial yang merupakan ciri unik lembaga pengarah di Malaysia. Ciri-ciri lembaga pengarah yang lain termasuklah struktur kepimpinan, bebas, pengarah berganda, pengarah dari keluarga pengasas dan kepakaran kewangan. Dua jenis pemilikan yang dipilih ialah pemilikan oleh pengarah dan institusi. KPK yang merupakan pemboleh ubah bergantung diproksikan dengan kualiti akru metrik. Sejumlah seratus tiga buah syarikat tersenarai di papan utama *Bursa* Malaysia yang kekal tersenarai sepanjang sebelas tahun dari tahun 1996 hingga 2006 disamping mempunyai data-data pemboleh ubah yang lengkap telah dipilih.

Syarikat kekal tersenarai dipilih bagi membolehkan penggunaan reka bentuk kajian yang meliputi pemerhatian yang seimbang, bertujuan agar penilaian secara objektif boleh dibuat ke atas implikasi reformasi urus tadbir korporat terhadap KPK syarikat. Analisa regresi dibuat secara berasingan bagi menunjukkan dua jenis reformasi yang berbeza iaitu perundangan (reformasi-I) dan institusi dan pengamalan yang baik (reformasi-II). Kajian ini menjangkakan bahawa pelaksanaan dua jenis program reformasi yang berbeza tersebut akan menghasilkan titik lengkok balas terhadap KPK syarikat (iaitu bertambah baik) serta akan memoderasi secara baik perhubungan statistik di antara kedua-dua pemboleh ubah tidak bergantung (lembaga pengarah dan pemilikan) dan KPK syarikat.

Hasil kajian menunjukkan bahawa majoriti (88% di dalam reformasi-I dan 75% di dalam reformasi-II jangka waktu analisa) pembolehubah lembaga pengarah dan pemilikan yang diuji di dalam kajian ini dikenalpasti sebagai penentu KPK yang signifikan (mengikut arah yang dijangkakan) di Malaysia. Hasil kajian analisa interaksi (menguji kesan moderasi oleh program reformasi) secara amnya menunjukkan kebolehan yang rendah bagi reformasi-I untuk memoderasi perhubungan di antara pembolehubah-pembolehubah penentu dengan KPK, berbanding reformasi-II. Ini secara tidak langsung mencadangkan keberkesanan moderasi yang lebih tinggi oleh reformasi-II. Kajian ini walau bagaimana pun gagal menjumpai sebarang bukti empirikal yang menunjukkan bahawa KPK syarikat telah bertambah baik selepas reformasi. Tiga alasan yang berkait dengan (1) keadaan ekonomi makro; (2) kepentingan urus tadbir korporat dalam menambah baik KPK syarikat; dan (3) kehadiran ciri-ciri urus tadbir korporat dan ekonomi yang unik di Malaysia telah dicadangkan untuk menerangkan hasil kajian tersebut.

Hasil ujian kepekaan mencadangkan bahawa, selain daripada beberapa perbezaan kecil dalam keputusan kajian, penemuan-penemuan utama di dalam kajian ini adalah teguh kepada spesifikasi pembolehubah alternatif dan jangka waktu kajian alternatif. Secara keseluruhan, kajian ini menyumbang kepada tahap penulisan ilmiah di dalam bidang urus tadbir korporat di dalam ekonomi yang baru muncul dengan membuktikan bahawa keberkesanan reformasi urus tadbir dalam memastikan KPK syarikat adalah sensitif kepada keadaan ekonomi dan pelbagai ciri-ciri unik urus tadbir dan sifat-sifat institusi.

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In the name of **ALLAH**, Most Gracious, Most Merciful.

All praise due to **ALLAH**, Peace be upon Prophet Muhammad (S.A.W).

O **ALLAH**, in humiliation, I beg Your forgiveness, for sins I have committed, intentionally as well as unintentionally.

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- ii. My late parents (May **ALLAH** SWT have mercy on them);
- iii. My wife, my one and only daughter, my siblings and my in law family members;
- iv. GSM-UPM lecturers and administrative staffs;
- v. All staffs of USM School of Management
- vi. The rest of the *Ummah* of Prophet Muhammad (PBUH)

If this moderate academic effort is considered as acceptable and successful, it is entirely by **ALLAH**'s grace and guidance. Otherwise, if it falls short of readers' expectations, I can only pray and patiently hope that **ALLAH** will forgive my imperfect efforts and judgments.

I certify that an Examination Committee met on **20th September 2010** to conduct the final examination of **Hairul Suhaimi b. Nahar** on his **Doctor of Philosophy** thesis entitled “**The Malaysian Corporate Governance Reform and Financial Reporting Quality**” in accordance with Universiti Pertanian Malaysia (Higher Degree) Act 1980 and Universiti Pertanian Malaysia (Higher Degree) Regulations 1981. The Committee recommends that the candidate be awarded the relevant degree.

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DECLARATION

I hereby declare that the thesis is based on my original work except for quotations and citations which have been duly acknowledged. I also declare that it has not been previously or concurrently submitted for any other degree at Universiti Putra Malaysia (UPM) or any other institutions.

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