The Effectiveness of Corporate Governance on Real Earnings Management in selected Malaysian Companies

By

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A Master Dissertation Submitted to the Postgraduate Studies, Othman Yeop Abdullah Graduate School of Business Universiti Utara Malaysia, in Partial Fulfilment of the Requirement for the Degree of Master of Science in Finance
DECLARATION

I hereby declare that the content of this thesis is solely based on my original work and has not been previously submitted for any other degree in Universiti Utara Malaysia or any other institutions. The quotations and citations used in writing this research have been duly acknowledged.

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ABSTRACT

The practice of real earnings management occurs at companies where investors’ protection is high and stringent corporate governance measures are put in place. The study examines the relationship between corporate governance attributes and real earnings management. In this study, real earnings management is measured using three proxies, abnormal discretionary expenses, abnormal production cost, and abnormal cash flow from operations. The corporate governance attributes examined are board structure characteristics and audit committee characteristics. The sample consists of top 100 companies rated high based on the Malaysia Corporate Governance Index 2011 (MCG Index) on best practices of corporate governance. Financial companies are excluded, resulting in a final sample of 78 companies. The relationships of board structure and audit committee are tested using Ordinary Least Square regression. The results reveal that certain corporate governance variables are effective in constraining real earnings management activities. The findings of the hypothesised variables, board structures, and audit committee. The study finds that only board size and directors expertise constrain earnings management, but none of the audit committee variables show significant relationships with real earnings management. It can be concluded that board size and directors expertise are constraining factors in constraining real earnings management. The finding of the study is important for market participants and policymakers in defining effective corporate governance mechanisms that could address the issue of real earnings management.
ABSTRAK

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CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Companies around the globe are mandated to produce financial statement in the form of annual reports at the end of their financial year. Financial statement of a company displays the picture of an organization’s outcome and consequence of its activities. Management often uses this report for planning and control. Of this information, reported earnings are important elements that reflect the past operations and predict the future. Reported earnings are the addition of cash flow from operation and accruals.

In preparing the financial statement various statutory requirements and regulatory rules are adhered to, such as company law, accounting standards, taxation law etc. Among the preparers of the reported earnings, managers and auditors of company play very magnificent roles and these roles may be influenced by the economic settings of the environment that they operate.

The reported earnings are metrics that portray company status, effectiveness of management and depict its economic realities and financial prospects. Reported earnings numbers are important and serve as a candle light in providing costly, applicable and pertinent information to users, be it internal and external (e.g., shareholders, employees, investors, debt holders, managers and financial analyst) in making business decisions.
The contents of the thesis is for internal user only
References


