CORPORATE CHARACTERISTICS AND VOLUNTARY DISCLOSURE OF MALAYSIAN LISTED CORPORATION

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ABSTRACT

The term " voluntary disclosure" has been variously defined to include reporting on profit forecast and projection, corporate achievement, corporate mission and value added statement. There are currently neither legal requirements nor accounting pronouncements to regulate disclosures in these aspects. In Malaysia quantified profit forecast disclosure is only required when a company issues a prospectus in an initial public offering. The purpose of the study was to investigate the level of Malaysian corporate voluntary disclosure and its association with size, profitability, institutional holdings and auditor's reputation. Data collected were analyzed using SPSS. The general findings showed that then level of company disclosure is lower than the external users considered desirable. Correlation study using Pearson Correlation indicated a statistical significant positive relationship between disclosures level and total assets, total equity, share capital and net profit for plantation and industrial products companies, while trading and services companies showed only a positive correlation between disclosure and sales turnover. Auditor's reputation shows no effect on voluntary disclosure for all three industries under review. Companies were willing to disclose only information that is not considered sensitive.

INTRODUCTION

Annual reports are the major medium used by listed companies to communicate information to outsiders. In Malaysia, every company incorporated under the companies act 1965, must comply with the act's provisions concerning accounting and reporting as they are legally enforceable.

The purpose of this article is to report on a study of four corporate characteristics that may, or may not have some influence over the level of voluntary disclosure. These four characteristics are the size of the company, the company's profitability, institutional holdings and auditor's reputation engaged in the audit.

The first step in the research design was to construct a list of items of information that are, or could be included in corporate annual reports. The list was then applied to a sample of annual reports and a disclosure index was calculated for each one. From this analysis, the following questions were tackled:

a) Does the size of a company have any impact on its level of voluntary disclosure?
b) Does the firm's profitability have any impact on the level of disclosure?
c) Does an auditor's reputation have any impact on the level of disclosure?
d) Does institutional holdings have any influence on the level of disclosure?

LITERATURE REVIEW

Economic theory, intuition and empirical evidence suggest that size of a company is likely to have positive influence on voluntary disclosure practices. Due to possible economics of scale in the production and storage of information, large companies tends to allocate relatively greater amount of resources to the production of information (Stigher, 1961; Alchian, 1969). Singhvi and Desai (1971) focused on the quality of disclosure in annual reports and found that it is influenced to a greater extent by the listing requirements of a stock exchange. Buzby (1974,1975) reported on the relationship between a subcomponent of adequate disclosure – the extent of selected items of information presented in annual reports-and two company characteristics. The results of his research indicated that the extent of disclosure was positively related to the size of company's assets and not the listing status of the company. He suggests that the opportunity cost of voluntary disclosure may be higher for small companies than for large companies. They may therefore, disclose less information than large companies.

It has been established that increased disclosure by a company reduces its cost of capital (Choi, 1973; Elliot and Jacobson, 1994), and since large companies rely more heavily on the securities market for external financing for their operations than smaller companies, it follows that large companies are more likely to have extensive disclosure than small companies (Shapiro, Wolf, 1972; Salamon & Dhaliwal, 1980). Finally empirical evidence confirms the hypothesized positive relationship between company size and disclosure (Cerf, 1961; Singhvi & Desai, 1971; Firth, 1979; Wallace, 1988; Cooke, 1989a, 1989b; Wallace et.al.1994; Meek, Gary K, Roberts, Clare B, 1995; Inchausti, 1997)

On the impact of auditing firms on disclosures, , it was found in the United Kingdom that there is no persuasive evidence that increased or decreased disclosure is associated with whether the auditing is from the" Big 8" or not (Firth, 1979). In Malaysia (Tan ,Zainal, Cheong, 1990) noted that there is no discernable difference between the influence of audit firm size on voluntary disclosure in the annual reports.

Proprietary costs vary across industries (Verrencchia, 1983). Therefore industry membership may exert an influence on voluntary disclosure. Cooke (1989,1991) finds mild evidence of an industry effect in his studies of Swedish and Japanese companies. Industries appear to be influential in some cases. (Meek, Gary K, Roberts, Clare B, 1995). Companies in the oil, chemicals and mining industry seem particularly inclined to provide non-financial information, such as those related to the environment, perhaps reflecting greater sensitivity toward social accountability issues

RESEARCH DESIGN

List of items

The first step in the research design was to construct a list of items of information that appear or could appear, in corporate annual reports. A review of relevant literature (Baker, 1970; Buzby, 1974,1975; Cerf, 1961; Chandra, 1974; Choi, 1973; Singhvi and Desai, 1971; Tan, Zainal and Cheong, 1990) was made in order to select the items to be included in the list.

This list contains those items that had been included in more than one study as being important for professional users, principally financial analysts. A review of several recent company annual reports was also used in order to refine the list. The final list of twenty-two items categorized into four categories.

Measuring The Disclosure Level

The company's annual reports were used in the computation of their disclosure indices. Published accounts for the financial year ended during 1998 were examined to establish whether disclosure of an item had occurred. The study set out to see whether each of the 22 items was thought to be present in every company was disclosed. In order to capture all voluntary information disclosed, the annual reports and accounts was thoroughly read through in its entirety as the disclosure could be in the chairman's statement, management review, director's report and notes to the accounts. It was also aware that some companies might disclose certain voluntary information in the form of statistical bar chart or pie chart. This type of disclosure was also taken into account and was regarded as quantitative data.

If an item was disclosed then the company received a one score and if the item was not disclosed then the company received a zero score. However, half credit was given if only partial information was disclosed, for example the firm only made a general statement about the "items". The unweighted scores for the individual items for each company were then totaled, and expressed as a percentage of the maximum score (which was 22) and this figure is known as the disclosure index for that company.

The voluntary disclosure score for each company is additive and unweighted. Unweighted scores are used for several reasons. First is subjectivity that would be involved in assigning weighs when user preferences are unknown (Chang, Most and Brain 1983). In addition it has been suggested(Spero, 1979) that companies better at disclosing "important" items are also better at disclosing "less important" items. Thus, companies would be scored the same way regardless of whether items are ranked or unranked. Unweighted scores have been used in other empirical studies (Cooke 1989). In addition, Chow and Wong – Boren (1987) find almost identical results using either ranked or unranked disclosure scores.

Sample Companies

A list of the main board Kuala Lumpur Stock exchange (KLSE) listed corporation is used as a sampling frame. Total populations of 444 companies listed on the main board were identified. For the purpose of this study, only three major industries were chosen, namely trading and services, industrial products and plantation sector. The sample for this study is made up of the followings:

1. 41 industrial products companies were randomly selected from the 94 companies of the main board listed in the KLSE
2. 42 trading and services companies were randomly selected from the 74 companies of the main board listed in the KLSE
3. 20 plantation companies from 39 companies listed in the KLSE

Annual reports released in 1998 by the companies in the above samples were obtained. These reports were used both for measuring their disclosure levels and for extracting information on their size (turnover, share capital, total assets, total equity), institutional holdings and their auditors.

DATA ANALYSIS

Correlation analysis using the Pearson Correlation Coefficient was used to reveal the magnitude and direction of relationship between independent variables and dependent variable of disclosure. Pearson correlation was chosen as it deals with interval and ratio data gathered in the study.

The hypothesis was tested using a multiple regression model. Multiple regressions is used to develop a self weighting estimating equation by which to predict values for dependent variable (disclosure) from the values for several predictor variables (IVs). Thus this study tries to predict companies' voluntary disclosure on the basis of size, auditors' reputation, profitability and institutional holdings.

RESULTS

The voluntary disclosure items disclosed

Table 1 lists twenty-two voluntary disclosure items used in the study. The study conducted was based on the 1998 annual reports of 103 listed companies from industrial products, trading and services and plantation sector. The result in table 2 indicates that:

a) Only one item (4.5%) was disclosed by more than 80% of the companies in the study. Disclosure by industry shows that the same item were disclosed by more than 80% of companies in trading, industrial and plantation sector.
b) Only four items (18%) were disclosed by more than 40% of the sample companies. The same four items were disclosed by more than 40% of the

companies in the trading and plantation sector while only three items (13.6%) were disclosed by more than 40% of industrial products companies.

c) Seven items (31.8%) were disclosed by fewer than 10% of the companies and three of these items (13.6%) were not disclosed by any company. These three items are:
   -profit forecast for the next year
   -statement of dividend policy
   -sales forecast for the next year
d) Disclosure of internal – strategic /predictive information items was very limited, with 3 of the 5 items which is categorized as strategic information not being disclosed by any company.
e) No single company disclosed more than 80% of the items, only one company disclosed more than 60% or 14 out of 22 items, and 20 companies disclosed no more than 2 items (i.e. less than 10%).

--------------------------Table 1--------------------------

The general findings reported above indicate that the level of company disclosure is lower than the external users considered desirable. The only company that had disclosed more than 60% of the twenty-two items had won an award in the National annual Report Award (NACRA) competition in the year 1997. Companies were willing to disclosed only information that is not considered sensitive. External users ranked the three items that were not disclosed by any company, as being in the 15 most important items to be disclosed in the previous studies. Studies carried out in Malaysia by Tan Zainal and Cheong(1990_) revealed that profit forecast and sales for the next year were ranked number 2 and 11 respectively in importance to external users. The result of non disclosure for these three items are consistent with the findings of Tan, Zainal and Cheong(1990); Mc Nally (1982); Buzby (1975) and Firth (1979).

Impact of size

The association of size and the level of disclosure are measured by Pearson correlation coefficient for each of the three industries. The result of the test is shown in table 2. These shows that there is a positive association between size measured in terms of total assets, share capital and total equity and the level of disclosure at 0.05 level for industrial products and plantation companies.

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Impact of auditors

The external auditors of each company in the three samples were extracted and they were categorized into those in the so-called " Big 6" (Arthur Andersen, Coopers & Lybrand, Peat Marwick, Price Waterhouse, Earnst & Young and Kassim Chan & Delloite) and others. The result in table 3 showed that there was no significant relationship in the disclosure scores between " Big 6" audited companies and those audited by smaller companies, for any of the samples. The results are consistent with Tan, Zainal and Cheong, 1990; and those derived in the U.K. (Firth, 1979). This however contrasts with Singhvi and Desai's research in USA where they found that the larger firms of auditors were significantly associated with greater level of disclosure.

---------------------------Table 3---------------------------

Impact of Profitability

Results from table 4 showed that there is a significant positive correlation at 0.05 significant levels between profitability in terms of net profit and disclosure for plantation and industrial products companies. Plantation companies showed a stronger correlation with Pearson rho of 0.716 compared to industrial product companies. Trading and services companies, reveal no significant correlation between profitability and disclosure.

---------------------------Table 4---------------------------

Institutional Holdings Effect

The test is carried out to see whether there is a significant correlation (positive / negative) between companies owned by majority institutional shareholders and level of disclosure.
The result from table 5 reveal that only plantation companies showed a significant positive correlation at 0.05 level between institutional holdings and disclosure. Other industry under review shows no significant correlation.

---------------------------Table 5---------------------------

Multiple Regression Analysis

Table 6 summarizes the regression equation runs with four corporate attributes of profitability, size, nature of holdings and auditors. The results of this model suggest that three corporate attributes have statistical significant effect on disclosures. While turnover, share capital and institutional holdings have a positive significant effect at 0.001 level, net profits and company's size in terms of total assets shows a significant negative effect at the 0.001 levels.

Profitability has been identified in previous studies, as capable of influencing the extent to which companies disclose information in their annual reports. Cerf (1961) suggested that profitability is a measure of management performance, and as such the management of profitable company is more to disclose information to support the continuance of their positions and performance related compensatory schemes that may be due to them.

The findings of this study that profitability measured in terms of net profit is negatively related to voluntary disclosure is inconsistent with signaling theory. This theory when applied in the present context, suggests that managers of profitable companies are more likely to disclose more in their annual reports to justify their salaries (Singhvi & Desai, 1971), and to signal their superior performance to the market (Wallace et al, 1994). However, it can also be argued that unprofitable companies will also be inclined to release more information in defense of poor performance. Indeed, Lang & Lundholm (1993, pp.250) note that the influence of a company's profitability level on disclosure can be positive, neutral or negative depending on its performance.

Pearson correlation study between net profit and voluntary disclosure for each industry however shows that there is a strong positive correlation between net profit and disclosure of industrial products and plantation companies at 0.005 significant levels. The association between net profit and disclosure of trading and services companies is however not significant (Pearson rho of 0.002). Perhaps, the industry bias might explain the negative association between net profit and disclosure in the model.

Similarly the negative effect of assets size on voluntary disclosure is inconsistent with the conclusion made by Mc Nally(1982). His research concluded that the size variable in terms of total assets is positively associated with voluntary disclosure.

Two other measures of size used in the study were sales turnover and share capital. Establishing a positive relationship between disclosure and turnover and share capital is consistent with previous study by Firth, 1979. The result of positive effect suggests that large companies are better in disclosing voluntary information, as their competitive advantage will not be weakened by such disclosure as it might be for small companies.

The findings that institutional holdings are positively related to voluntary disclosure are consistent with agency theory. In the context of disclosure studies, this theory suggests that companies whose equity shares are predominately held by insiders tend to disclose less information in their annual reports. Institutional holdings companies tend to be more in the public eye and attract more interest from government bodies, and they may therefore are more transparent in disclosure thinking that this will allay public criticism or government intervention in their affairs. Results by industry however show that only plantation companies have a strong positive association between institutional holdings and disclosure at 0.001 levels. Other industry shows no association

---------------------------Table 6--------------------------

CONCLUSION

The overall results of the study shows that the level of voluntary disclosure is still low despite the importance put by professional users. Disclosure practice in Malaysian listed corporation is still at mandatory level with the exception of a few companies who disclose more than 50% of the index items.

The correlation studies employed showed that there is a significant relationship between the companies disclosure level with the company's share capital, total assets, turnover, net profit as well as institutional holdings. There is also no evidence that greater or lower disclosure is associated with whether the auditing firm is from the "Big 6" or not.

Even though larger companies do exhibit greater disclosure, when compared with levels desired by professional external users it is low. It may be therefore necessary to extend the variety of items subject to mandatory disclosure requirements or for the government to exert more pressure on companies for greater transparency in presenting their annual reports. It is also suggested that the KLSE, the organizer of National annual Corporate Awards (NACRA), placed greater emphasis on voluntary disclosure besides their compliance with mandatory disclosure requirements.

Table 1 : Analysis of voluntary disclosure

Items of Information	% of companies disclosing (total)	Number of companies disclosing			Percentage of companies disclosing		
		Trading	Indust. Product	Plantation	Trading	Indust. Product	Plantation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
A. Internal – operation and management information							
Statements of company's objectives and policies	7.8	4	2	2	9.5	4.9	10
Historical summary of operating and financial data	68.9	32	28	11	76.2	68.3	55
Corporate mission	15.5	5	7	4	11.9	17.1	20
Corporate achievement	66	33	22	13	78.6	53.7	65
Management profile	14.6	7	4	4	16.7	9.8	20
Corporate calendar of significant events	48.5	27	12	11	64.3	29.3	55
B. Internal – strategic/ predictive information							
Profit forecast for the next year	0	0	0	0	0	0	0
Statement of dividend policy	0	0	0	0	0	0	0
Sales forecast for the next year	0	0	0	0	0	0	0
Breakdown of expenses into fixed and variable(past years)	1	0	0	1	0	0	5
Statement of interest and principal due on long term debt	4.9	3	2	0	7.1	4.9	0

Items of Information	% of companies disclosing (total)	Number of companies disclosing			Percentage of companies disclosing		
		Trading	Indust. Product	Plantati on	Trading	Indust. Product	Plantati on
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
C. External information							
Future economic outlook for the company	84.5	36	33	18	85.7	80.5	90
Future economic outlook of industry	24.3	13	8	4	31	19.5	20
Share of market in major product areas	1.9	2	0	0	4.8	0	0
General information on the impact of inflation on financial results	35	13	16	7	31	39	35
Discussion of the major factors which will influence next year's results	33	14	13	7	33.3	31.7	35
Information on major industry trends	9.7	8	2	0	19	4.9	0
Analysis of share prices	15.5	4	6	6	9.5	14.6	30
D. Corporate Social Reporting							
Employees welfare	19.4	9	7	5	21.4	17.1	20
Community involvement activities	23.3	16	3	5	38.1	7.3	25
Environmental protection	11.7	4	4	4	9.5	9.8	20
Product or service improvement or contribution	26.2	10	14	3	23.8	34.1	15

Table 2: Impact of Size on Voluntary Disclosure

Table 2
Impact of size on voluntary disclosures

(1) Size – Sales Turnover

	Sample 1	Sample 2	Sample 3
	41 Trading & services companies	42 Industrial products companies	20 Plantation companies
Pearson (rho)	0.445**	0.242	0.144
Significant (2-tailed)	0.004	0.127	0.545

(2) Size – Total Assets

	Sample 1	Sample 2	Sample 3
	41 Trading & services companies	42 Industrial products companies	20 Plantation companies
Pearson (rho)	0.281	0.475**	0.667**
Significant (2-tailed)	0.075	0.002	0.001

(3) Size – Total Equity

	Sample 1	Sample 2	Sample 3
	41 Trading & services companies	42 Industrial products companies	20 Plantation companies
Pearson (rho)	0.234	0.622**	0.652**
Significant (2-tailed)	0.141	0.000	0.002

(4) Size – Share Capital

	Sample 1	Sample 2	Sample 3
	41 Trading & services companies	42 Industrial products companies	20 Plantation companies
Pearson (rho)	0.189	0.575**	0.769**
Significant (2-tailed)	0.235	0.000	0.000

** Significant at 0.05 levels

Table 3: Auditor's Reputation - Effect on Disclosure Index

Table 3
Auditor's Reputation - Effect on Disclosure Index

	Sample 1	Sample 2	Sample 3
	41 Trading & services companies	42 Industrial products companies	20 Plantation companies
Pearson (rho)	0.137	0.037	0.014
Significant (2-tailed)	0.393	0.820	0.953

Table 4 :Impact of Profitability on Disclosure Index

Table 4
Impact of Profitability on Disclosure Index

	Sample 1	Sample 2	Sample 3
	41 Trading & services companies	42 Industrial products companies	20 Plantation companies
Pearson (rho)	0.002	0.563**	0.716**
Significant (2-tailed)	0.989	0.000	0.000

** Significant at 0.05 level

Table 5 : Impact of Institutional Holdings on Disclosure Index

Table 5
Impact of Institutional Holdings on Disclosure Index

	Sample 1	Sample 2	Sample 3
	41 Trading & services companies	42 Industrial products companies	20 Plantation companies
Pearson (rho)	0.144	0.156	0.678**
Significant (2-tailed)	0.369	0.319	0.001

** Significant at 0.05 levels

Table 6 : Effects of Corporate Attributes on Voluntary Disclosure.

Model 1				Collinearity statistics	
Variables investigated	Beta	T	Significant	Tolerance	VIF
(constant)		4.400	.000		
Net profit	-.475	-4.612	.000	.595	1.682
Total assets	-.964	-4.452	.000	.134	7.440
Annual turnover	.837	4.068	.000	.149	6.716
Share capital	.499	5.249	.000	.696	1.437
Institutional holdings	.513	4.494	.000	.483	2.071
Auditor	.032	0.401	.689	.972	1.028
R^2	0.402				
F statistics	10.630				

Model 1:

VDS_j = -. 475 net profit -. 964 total assets + .837 turnover + .499 share capital + .513 institutional holdings + .032 auditors

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