

**THE EFFECT OF BOARD STRUCTURE AND INSTITUTIONAL OWNERSHIP
ON EARNINGS MANAGEMENT**

By

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**Thesis Submitted to the Graduate School of Management,
Universiti Putra Malaysia, in Partial Fulfillment of the Requirement for the Degree
of Master of Science**

June 2006

Abstract of thesis presented to the Senate of Universiti Putra Malaysia in partial fulfillment of the requirement for the degree of Master of Science

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The study examines the role of outside directors and institutional shareholders in constraining the earnings management activities. A sample of 613 firms from construction, industrial products and consumer products sectors were selected from the Main Board in Bursa Malaysia. The time period covered for this study was from 2001 to 2003. The Modified Jones Model with cross sectional approach was employed in this study. The finding shows that the magnitude of earnings management in Malaysian listed firms was approximately 16% of the previous year total assets. Most firms manage the earnings upward rather than downwards. No relationship was observed between the degree of earnings manipulation and the proportion of outside directors and institutional shareholders. This is inconsistent with most studies which provide evidence that outside directors and institutional shareholders are effective corporate governance mechanisms in constraining the earnings management. However, there is weak evidence to show that

outside directors have some effect in curbing the earnings management in the construction sector.

The findings suggest that outside directors have the ability to constrain the earnings management as indicated in the construction sector. Adding more outside directors in the board and having institutional shareholders may not reduce earnings management practices if the ownership of a firm is highly concentrated and the process of selecting outside directors is not clearly stated and transparent.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi sebahagian keperluan untuk ijazah Master Sains

KESAN STRUKTUR LEMBAGA PENGARAH DAN INSTITUSI PEMEGANG SAHAM KE ATAS PENGURUSAN HASIL

Oleh

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Kajian ini menyelidik keberkesanan peranan pengarah luaran dan institusi pemegang saham dalam menyekat pengurusan hasil. Jumlah sampel sebanyak 613 buah syarikat dari sektor pembinaan, barang industri, dan barang pengguna dipilih dari Papan Utama Bursa Saham Malaysia. Kajian ini merangkumi tahun 2001 ke 2003. Modified Jones Model dengan pendekatan “cross sectional” digunakan dalam kajian ini. Hasil kajian menunjukkan purata pengurusan hasil di Malaysia ialah sebanyak 16% atas jumlah aset pada tahun lepas. Didapati bahawa syarikat lebih cenderung meningkatkan hasil daripada menurunkan hasil. Daripada keputusan yang diperolehi, tiada hubungan yang wujud di antara pengarah luaran dan institusi pemegang saham dengan pengurusan hasil. Keputusan ini tidak seiringan dengan kebanyakan kajian yang membuktikan bahawa pengarah luaran dan institusi pemegang saham merupakan mekanisme kawalan korporat yang efektif dalam menyekat pengurusan hasil. Walaubagaimanapun wujud hubungan

yang negatif antara pengaruh luaran dengan pengurusan hasil di sektor pembinaan tetapi buktinya amat lemah.

Adalah dicadangkan bahawa pengaruh luaran berupaya menyekat pengurusan hasil dalam sektor pembinaan. Penambahan bilangan pengaruh luaran dan institusi pemegang saham berkemungkinan tidak dapat mengurangkan praktik pengurusan hasil jika hakmilik syer terlalu memusat kepada sesetengah pihak dan proses memilih pengaruh luaran tidak dinyatakan dengan jelas dan lutsinar.

ACKNOWLEDGEMENTS

First and Foremost, I would like to express my deepest gratitude to Assoc. Prof. Loo Sin Chun for his continuous guidance, support and assistance throughout the thesis preparation process. I sincerely appreciate his encouragement and insightful suggestions given to complete this thesis.

My gratitude extends to my committee member, Prof. Shamsheer Mohamad Ramadili for giving me invaluable comments, suggestions and commitment of reviewing in improving this thesis.

My heartfelt thank to my beloved family members who give their unbounded encouragement and support throughout my studies in Universiti Putra Malaysia. To my boyfriend, Kent for his consideration, intellectual and spiritual support. Without him I probably cannot go through this hectic research journey.

Last but not least, my special thanks to my coursemates: Rajes, Shakirah and Zetty for their sharing and encouragement in the research process.

I certify that an Examination Committee met on **26 April 2006** to conduct the final examination of **Wong Shi Yang** on her **Master of Science** thesis entitled “**The Effect of Board Structure and Institutional Ownership on Earnings Management**” 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. Members of the Examination Committee are as follows:

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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 UPM or other institutions.

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