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The Moderating Impact of the Big-4 on Audit Committee and Earnings Management: During Pre-Post IFRS Adoption in Malaysia

Mohamed Salem M.S. Bayou(1)

Magdi Ahmed Fathi El-Bannany(2)

Mohamad Ali Bin Abdul Hamid (3)

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Abstract:

This study investigates the moderating impact of Audit Quality (AQ) on Audit Committee (AC) and Financial Reporting Quality (FRQ) during pre-post IFRS full adoption. It argues that the AC improves FRQ but subject to the choice of auditor. The study considers several variables on its measurements related to dependent, independent, moderate, control variables which include measures such as discretionary accruals, the yearly number of AC meetings and the dummy variable. AQ is measured by a firm's auditor choice of the Big-4 and Non-Big 4 as an indication for the demand for high/low quality financial reporting. Using 567 listed firm-year observations from 2009 to 2015, investigations were deducted by examining the statistical significance difference during pre-post IFRS full adoption, using multiple regression analysis and paired sample t-test. The findings show that the Big-4 choice increases the relationship on the AC and FRQ when companies are adopting IFRS. The level of difference on earnings management practice was not significant. However, the result shows that IFRS full adoption have limited managerial discretion and the possibility for Earnings Management for Malaysian companies.

Keywords: IFRS Full Adoption, Audit Quality, Audit Committee, Earnings Management.

(1) The Libyan Academy Misurata (Misurata - Libya)
drmagdi.e@uaqu.ac.ae

(2) Faculty of Business - Ain Shams University (Cairo - Eygpt)

(3) Purta Business School (Serdang - Malaysia)

1. Introduction:

Financial reporting plays an important role in effectively communicating firms' comic performance (Healy & Wahlen, 1999). In fact, a consequence of the 1997/1998 financial crisis in South East Asia and the subsequent episodes at Enron in 2001 and WorldCom in 2002 was that public attention turned towards managers' opportunistic utilization of earnings management (EM) (Jiraporn, Miller, Yoon, & Kim, 2008). Those scandals led to worries about the quality of financial reporting and the effectiveness of ACs in protecting shareholders' interests (Rezaee, Olibe, & Minmier, 2003). Even Malaysia has not been insulated from high-profile scandals involving big companies such as Transmile Group Bhd, Malaysian Airlines Systems, LFE Corporation Berhad, Promto Bhd and MEMS Technology Bhd (Hasnan, Rahman & Mahenthiran, 2013). Evidently, this series of corporate scandals has caused a lot of damage to investors' confidence in the capital market (Kallamu & Saat, 2015) leading to questions about the oversight responsibilities of the AC on financial reporting (HassabElnaby, Said, & Wolfe, 2007). Furthermore, Hasnan et al. (2013) have argued that fraudulent financial reporting usually begins as EM and exhausts most aggressive accounting principles and grows over time to become a major problem.

Since it is difficult to recognize the indications of FRQ, according to Cohen et al. (2004), factors such as EM, a restatement of financial performance, and fraud are the focal point of studies to delineate FRQ. One of the techniques, advocated by Salleh and Haat (2014) to counter financial scandals is to improve the reporting of EM through improvement in corporate governance (CG) quality. In this regard, CG has been identified as playing a crucial part in ensuring the uptake of ethical practices within an organization across all its operations. It also helps imbue the staff with moral accountability. From here, this research uses the AC as one mechanism of CG as a measure to examine the quality of financial reporting.

The Malaysian Code of CG (MCCG) (2001) and the 2007 revised code emphasized that the AC should ensure high-level internal control and risk management systems. Further, the MCCG (2012) and MCCG

(2016) highlighted that the AC should ensure that the relevant standards of reporting are observed when producing financial reports.

Although there is a rich body of literature on ACs and EM issues in Malaysia, discussions of the relationship between ACs and FRQ (proxies by EM-DACC) have not been extensive. Several previous studies, in several different contexts, have investigated the influence of ACs on EM. However, the empirical evidence is rather inconsistent. For instance, Soliman and Ragah (2014), Al Momani and Obeidat (2013) and Inaam & Khamoussi (2016) documented that ACs and AQ have significantly negative associations with discretionary accruals (DACC) - that is, ACs and AQ effectiveness on reducing the extent of EM and limit monitoring on the quality of financial reporting. Johl, et al. (2013) also analyzed companies listed on Bursa Malaysia for 2009-2010, and the first assessment showed that AQ was positively associated with EM, signifying reduced FRQ. In contrast, Hasan (2017) investigated the impacts of AQ on ACs and FRQ in Malaysia. The results of the study showed that the AC had mixed findings with a significant and non-significant relationship with FRQ. Based on the above findings, audit committee independence, financial expertise and size are not significant, except from audit committee meeting (ACMEET) which is supported and significant. However, much earlier Fan and Wong (2002) found that accounting earnings are lower for East Asian firms including Malaysia. This highlights the need for re-examining the impact of governance monitoring on the quality of financial reporting.

At the same time, other research has generally indicated an improvement in accounting quality for firms reporting under IFRS (Barth et al., 2008; Chen et al., 2010) with contradictory evidence observable for firms from strong enforcement countries (Ahmed, et al., 2013). However, several previous studies conducted by Ball et al, (2003), Leuz (2003), Christensen et al. (2015), Wieczynska (2015) and Gellings (2017) show the effectiveness of IFRS adoption. Therefore, limited role of accounting standards determines the reporting quality and highlights the importance of the firm’s reporting incentives.

Moreover, previous research was conducted by Wan Abdullah et al.

(2017) regarding mandatory IFRS full adoption in Malaysia to examine the effects of IFRS full adoption on the quality of financial reporting. This study was also aimed to provide evidence of the effect of IFRS adoption and EM but limited to the construction industry. In this respect, the results revealed that there is a significant difference between the level of EM during the years before and after the adoption of IFRS in Malaysia.

Gellings (2017) documented that IFRS is considered to require disclosure of more information. Therefore, the relationship between mandatory IFRS adoption and AQ shows a positive relationship, which decreases EM. In considering IFRS adoption, FRQ may have various impacts - especially on AQ and cost increase. This is because of the greater effort, knowledge, and information systems needed to implement new standards. These increased audit efforts are mainly driven by two factors according to DeGeorge et al. (2012). First, auditors have to become knowledgeable about the new standards, so they can assess whether financial statements are in line with these standards. Secondly, auditors face more risks due to IFRS adoption in terms of chances of materially misstated financial statements (Love & Eickemeyer, 2009) and the litigation risk associated with this materially misstated financial statement (Diehl, 2010).

The paper is organized as follows: first, the problem of the Study which is followed by research motivation and objectives of the study. The literature review and hypotheses development are discussed in detail in section 4. This is followed by section 5 related to research models and variables measurement. Then, it discusses data analysis and findings in section 6. The last section provides conclusion, contribution and implication for future research.

2. Statement of the problem:

This study examines the moderating impact of AQ on AC to improve the reporting of EM through improvements in CG quality. It also uses the AC as one instrument of CG as a measure to examine FRQ and to understand the weak relationship between the AC and EM. However, a weak AC and/or FRQ may lead to difficult IFRS implementation process.

Thus, this study argues about and concentrates on the analysis of AC and EM during pre-post IFRS full adoption in Malaysian companies.

3. Research Motivation and Objectives:

This study is meant to investigate the moderating impact of AQ on AC and FRQ during pre-post IFRS full adoption. This study is also aimed to provide empirical evidence of the effect of mandatory IFRS full adoption in Malaysian companies in the relationship between AC and FRQ (EM-DACC proxy). Overall, this is a unique study in the Malaysian market and Asian region in the sense that it investigates whether IFRS full adoption has limited managerial discretion and the possibility of EM for Malaysian companies.

Extrapolating from the above paragraphs, the paper's objectives are: Firstly, to investigate the impact of mandatory IFRS full adoption on the relationship between AC and EM in Malaysian companies. This would limit EM practice in highlights of governance monitoring on the quality of financial reporting. Secondly, to explore the impact of mandatory IFRS adoption when AQ moderates the relationship between the AC and EM. Thirdly, to examine the level of EM practices pre-post IFRS full adoption in Malaysia. It is expected that the study will make important contributions to practice in its implication for regulators and standard setters of Financial Reporting Standards, given that CG practices in Malaysia has its own peculiar characteristics compared to other emerging and developed economies.

4. Literature Review and Development of the Study Hypotheses

4.1. Literature Review

4.1.1. Financial Reporting Quality (FRQ) and Earnings Management (EM)

The quality of financial reporting has two main aspects: AQ, and the quality of reported earnings. The present study focuses on earnings quality as a component of FRQ. This FRQ model uses part of the discretionary total accruals (TAC) (as well as non-discretionary) as a proxy for EM. This study also expands DACC as an EM measure, as mentioned in prior studies, which proposes and improves this measure. Healy and Palepu (2001) highlighted that companies offered the disclosure of structured financial reports, inclusive of the analysis and discussions of management, financial statements, and footnotes on financial performance as well as further regulatory filings. Furthermore, some of the firms take part voluntarily in communication activities; for instance, reports by corporate bodies, internet sites, press releases, forecasts by management, conference calls, and presentations by analysts. Disclosures of various companies are also available through information intermediaries like the financial press, industry experts, and financial analysts. Cascino and Gassen (2010) emphasized that FRQ is in compliance with generally accepted accounting standards.

4.1.2. Effect of Audit Quality as a moderator between Audit Committee and Earnings Management pre-post IFRS full adoption

Some previous studies have shown that adopting IFRS has brought benefits in the form of higher quality financial statements. Barth, et al. (2008) found evidence that after adopting IFRS, companies have less EM, exhibit more timely loss recognitions, and provide more value relevance – all qualified as higher quality financial statements. This is based on the fact that the new standards fill in the gaps in local accounting regulations by providing recognition and measurement rules for certain issues that had not been addressed in some countries. Klein (2002) also gave evidence that a non-linear negative relation is found between audit committee independence (ACIND) and earnings manipulation. Specifically, a significant relation is found only when the AC has less than a majority of independent directors. Barth et al. (2008) further explored the quality of accounting amounts for firms adopting IFRS. They also documented that firms with higher quality accounting are less subject to opportunistic managerial discretion. This is because DACC are created due to management decisions and not due to normal operational activities. Consequently, the manager can use this to manipulate reported income, that is, if EM has taken place. Balsam et al. (2003) and Krishnan (2003) find that an increase in DACC is associated with lower AQ because there is a higher likelihood of EM.

4.2. Development of the Study Hypotheses

4.2.1. Relationship between Audit Committee and Earnings Management

a. Audit Committee Independence (ACIND)

Vicknair, Hickman and Carnes (1993) and Choi, Jeon and Park (2004) found that ACs are a significant factor in inhibiting financial statement fraud. Some studies found that ACIND correlated negatively with EM (Soliman & Ragab 2014; Habbash 2010). However, Alves (2013) found a positive association between EM and ACIND. Other studies found that the independence of the AC was not significantly related to EM (Rahman & Ali 2006, Habbash et al. 2013, Hamdan et al. 2013). Hasan (2017) provided empirical evidence on the relationship between ACIND and FRQ in Malaysia. The results show that ACIND has no significant relationship with EM. Hence, it is hypothesised that:

H1a: *There is a significant negative relationship between Audit Committee Independence and earnings management during pre-IFRS full adoption.*

H2a: *There is a significant negative relationship between Audit Committee Independence and earnings management during post-IFRS full adoption.*

b. Audit Committee Financial Expertise (ACFEX)

Although independent directors with financial backgrounds might be good in monitoring with intentions, it is desirable to have ACs who have financial expertise to monitor the financial statements that have sophistication in financial matters to detect financial fraud. Previous research found that ACFEX has a significant effect on EM (Habbash, et al. 2013 and Rahman and Ali 2006). However, Hasan (2017) contradicted the findings of Habbash, et al. (2013) and Rahman and Ali (2006) where no significantly negative relationship between ACFEX and EM was found. Therefore, the following hypothesis is formulated:

H1b: *There is a significant negative relationship between Audit Committee Financial Expertise and earnings management during pre-IFRS full adoption.*

H2b: *There is a significant negative relationship between Audit Committee Financial Expertise and earnings management during post-IFRS full adoption.*

c. Audit Committee Meeting (ACMEET)

CG literature might support the proposition that frequency of meetings of ACs extensively reduces EM. ACs are intended to ensure constant communication among the board, internal auditors, and external auditors so that there are frequent ACMEETs. Chang and Sun (2009), Lin et al. (2006) and Xie et al. 2003) argue that increased frequency of ACMEETs is related to a decrease in discretionary current accrual levels. Previous research deemed that the frequency of meetings of ACs was like a signal of the diligence practiced by the members of AC (Klien 2002; Habbash 2010; Habbash et al.2013). In contrast, Hasan (2017) documented that ACMEETs are not significantly related with EM. These findings are similar to Rahman & Ali (2006), Baxtr & Cotter (2009), and Habbash (2010). Subsequently, this study can support the proposition that increased ACMEET frequency does in fact extensively reduce EM. The hypothesis is below:

H1c: *There is a significant negative relationship between Audit Committee Meetings and earnings management during pre-IFRS full adoption.*

H2c: *There is a significant negative relationship between Audit Committee Meetings and earnings management during post-IFRS full adoption.*

d. Audit Committee Size (ACSIZE)

Sharma & Kuang (2014) study and other studies found that the AC’s larger size does not considerably reduce EM. This equates to a vast majority of studies (Habbash, 2010; Alkadi et al., 2012; Habbash et al., 2013; Hasan, 2017) that failed to discover a major impact on the size of the AC on EM. However, since any relationship with statistical significance is absent, the coefficient has taken a negative directional sign. This is assuming that the ACs' larger size can reduce EM considerably. This led to formulating the hypothesis as:

H1d: *There is a significant negative relationship between Audit Committee size and earnings management during pre-IFRS full adoption.*

H2d: *There is a significant negative relationship between Audit Committee size and earnings management during post-IFRS full adoption.*

4.2.2 Audit Quality

In the agency theory literature, it is suggested that both the auditing firm and its clients benefit from such disclosure. The choice of an external auditor especially serves to increase company value. This choice is an indication to the investors of the high quality of the annual reports. Audit firms may capitalize on this greater disclosure to prove to outsiders that their audit is of higher quality (DeAngelo, 1981). Much of the AQ literature derives from DeAngelo's (1981) documenting of AQ as "the probability that an auditor will both discover a breach or material misstatement in the accounting systems or financial statements, and, further, report the breach." This definition has two elements: auditor expertise, which determines the likelihood that an auditor discovers material misstatements in the financial statements, and auditor objectivity/independence, which is related to the likelihood that an auditor will correct these misstatements when it is discovered (Knechel, 2016). Therefore, the following hypothesis for empirical testing is proposed:

H3: *Audit Committee is more strongly negative related to earnings management and Audit Quality as moderator when companies mandatorily adopt IFRS*

Chua, Cheong and Gould (2012) stated that the mandatory adoption of IFRS in Australia has resulted in better accounting quality than under the previous Australian Generally Accepted Accounting Principles (GAAP). Barth et al. (2008) revealed that a lower level of EM when firms adopt IFRS, where there was more timely loss recognition and more value relevance of earnings, all of which provides evidence of higher accounting quality. This empirical evidence indicated that the pervasiveness of EM was reduced by way of smoothing, while the timeliness of loss recognition has improved as well as the value relevance of financial statement information. Therefore, the following hypothesis is formulated:

H4: *There is a significant difference between audit quality, audit committee and earnings management practices during pre-post IFRS full adoption on Audit Quality*

5. Research Models and Variables Measurement:

5.1 Variables Measurement

Table 1 Shows measurement of variables including independent variables, dependent variables and control variables.

Table 1: Variables measurement

No.	Variables	Measures
Dependent:		
1	Earning Management (EM)	*Discretionary Accruals* (DACC) with Modified Jones Model [Dechow, et al., 1995]
Independent:		

2	Audit Committee Independence (ACIND)	The proportion of independent non-executive directors in the Audit Committee to total committee members (Total number of independent members in AC). [Beasly (2000), DeFond and Jiambalvo (1991), Habbash (2010)]
3	Audit Committee Financial Expertise (ACFEX)	Total number of AC members who had both financial and accounting backgrounds. [Chtourou, et al (2001), Abbott, et al (2004), Bedard, et al (2004), Choi et al (2004)]
4	Audit Committee Meeting (ACMEET)	The yearly number of Audit Committee Meetings. [Raghunandan & Rama (2007), Habbash (2010)]
5	Audit Committee Size (ACSIZE)	Total number of members on the Audit Committee [Lin, et al (2006), Adams & Mehran (2011)]
Moderate:		
6	Audit Quality	Dummy Variable, 1 if a company is audited by a Big-4 auditor and 0 if a company is not audited by Big-4 auditor. [Kim et al, 2012]
Control:		
7	Board Size (BRDSIZE)	The number of directors on the board. [Rahman & Ali (2006), Hashim & Devi (2008), Habbash (2010)]
8	Firm Leverage (FRMLEV)	Total long-term debt divided by total assets. [Hodgdon et al (2009), Dimitropoulos & Asteriou (2010)]

Most of the Earnings Management literature uses discretionary accruals as a proxy for EM. The current research, FRQ employs DACC as a proxy for EM. Earnings Management is the value of discretionary accrual or a change in accounting methods. To measure EM, proxied by value of DACC, the Modified Jones model (Dechow, et al 1995) was used to measure the level of EM or DACC. This model uses TAC classified as discretionary component (DTAC) and non-discretionary (NDTAC). Defined as follows:

TAC = NDTAC + DTAC

Description:
TAC = Total accrual period t
NDTAC = Value of non-discretionary accruals
DTAC = Discretionary Accrual

First measured TAC before DACC. Under the cash flow approach, TAC are measured as follows:

$TACC_{it} = EBXT_{it} – OCF_{it}$.. (1)

where:
$EBXT_{it}$ = earnings before extraordinary items and discontinued operations period t
OCF_{it} = operating cash flow for period t

$TAC_t / TA_{t-1} = a_1 [1/TA_{t-1}] + a_2 [\Delta REV_t / TA_{t-1}] + a_3 [PPE_t / TA_{t-1}] + \varphi$……...(2)

$NDTAC = \alpha_1 [1/TA_{t-1}] + \alpha_2 [(\Delta REV_t - \Delta REC_t) / TA_{t-1}] + \alpha_3 [PPE_t / TA_{t-1}]$…....(3)

$DTAC = AC_t/TA_{t-1} - NDTAC$…………………………………………..........................(4)

Where:
TAC = Total accruals in period t
NDTAC = value of non-discretionary accrual
DTAC = Discretionary accrual
REV Δ t = change in net sales in period t
REC Δ t = change in period t net receivables
PPE = Property, Plan, and Equipment
a 1 a 2 a 3 = coefficient of regression equation (2)
α 1 α 2 α 3 *= Fitted coefficients obtained from the regression equation (2)*

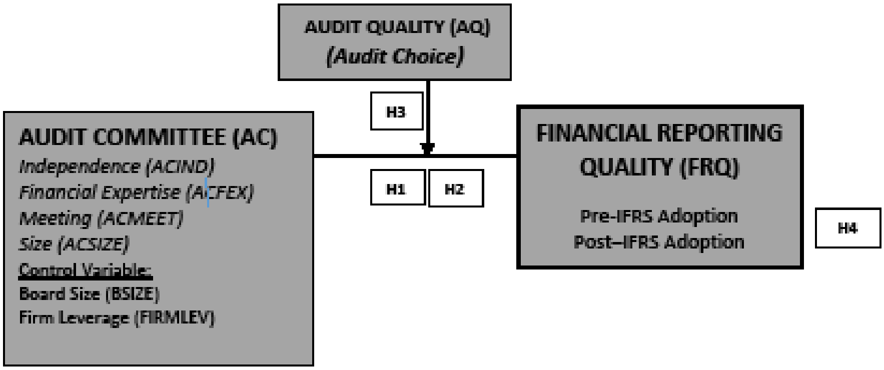

Figure 1. Theoretical Research Framework

5.2.Data and Sample

This study focuses on the analysis of AC and EM across two main time periods: the pre-IFRS mandatory adoption and the post-IFRS mandatory adoption period. The pre-IFRS full adoption period extends from 2009 through 2011 and is classified as “Pre-IFRS full adoption”, and the post-IFRS full adoption period extends from 2012 through the 2015 and is classified as “Post-IFRS full adoption”.

The data collection in this study is laid out in several steps: Firstly, it collects the list of all trading companies that were consistently and continuously quoted on the Bursa Malaysia published from 2009 to 2015. Secondly, it identifies companies that completely published their financial statements during the observation period of 2009-2015. Financial statements for 2008 were used to calculate the excess or difference with the previous year when calculating the EM variable. Thirdly, identifying companies that had incomplete data on variables of interest required in this study. The sample chosen in this research relied on a predetermined criterion which summarizes the process of the selection procedure (as shown in Table 2).

Table 2: Sample Selection Based on Selection Procedures

No	Items	Companies	(%)
	Total number of trading companies consistently listed on Bursa Malaysia from 2009-2015	162	100.00
2.	Companies with incomplete Financial Statement published during 2009-2015	(16)	9.87
3.	Companies that do not report on variables used in this study (ACIND, ACFEX, ACMEET, AC-(SIZE, Control Variables: BRDSIZE, FRMLEV	(65)	40.13
	Total Sample (Retain /Used data for further (analysis	81	50.00
	(Total Observations (7 years x 81 companies	567	

* Companies consistently listed on Bursa Malaysia from 2009-2015

After compiling data for all necessary variables, 81 companies were found to have complete data for all the variables required. For seven years, a total of 567 observations were analysed.

5.3. Multiple regression

Multiple regression is used in this study to explore the dependent and independent variables that are related. There are two models of Ordinary Least Squares regression used to test the proposed hypotheses (H1 and H2) and using the paired sample t-test to examine the statistical significance of differences between pre-post IFRS full adoption (H3) and (H4). This formula for hypothesis testing is as follows:

Pre-Post IFRS full adoption Equation *(H1 & H2)*

$DACC_{i,t} = \alpha 0 + \alpha_1$ ACIND $+ \alpha_2$ ACFEX $+ \alpha_3$ ACMEET $+ \alpha_4$ ACSIZE $+ \alpha_5$ BRDSIZE $+ \alpha_6$FRMLEV $+ \varepsilon$...(5)

Pre-Post IFRS full adoption Equation *(H3 & H4)*

$DACC_{i,t} = \alpha 0 + \alpha_1$ ACIND $+ \alpha_2$ ACFEX $+ \alpha_3$ ACMEET $+ \alpha_4$ ACSIZE $+ \alpha_5$ AQ+

α_6ACIND*AQ+ α_7 ACFEX*AQ+α_8ACMEET*AQ+ α_9 ACSIZE*AQ+ α_{10}BRDSIZE + α_{11} FRMLEV + ε…………………………..………………… (6)

6. Data Analysis and Findings

6.1. Descriptive Statistics

Test results of descriptive statistics pre-post IFRS full adoption and descriptive statistics each period can be seen in the following Table 3, Table 4 and Table 5:

Table 3 summarizes the descriptive statistics for the dependent, independent, moderate and control variables for all observational data. Based on Table 3, the minimum, maximum, mean and standard deviation for all 567 data observations is presented. The minimum value for DACC is -1.2562, and maximum value for FIRMLEV is 6302. The standard deviation for all variables is smaller than the mean value, which suggests that the data is reasonable because the changes of data collectively do not vary much. DACC's standard deviation value (0.2426) is higher than the mean value (-0.2194), this is because the firms have variation in DACC value.

Table 3: Descriptive Statistics Pre-Post IFRS full adoption

Descriptive Statistics					
	N	**Min**	**Max**	**Mean**	**Std. Dev**
ACIND	567	2	5	2.91	0.803
ACFEX	567	1	5	2.47	0.871
ACMEET	567	3	16	5.18	1.630
ACSIZE	567	3	8	3.50	0.718
DACC	567	-1.2562	0.6974	-0.2194	0.2426
AQ	567	0	1	0.74	0.446
BSIZE	567	4	16	8.22	2.388
FIRMLEV	567	2	6302	2110.97	1651.557
Valid N (listwise)	567				

Notes: The table reports summary statistics (minimum, maximum, mean, standard deviations and numbers of observations) for a number of variables for all of our sample firm-year observations using data for both periods immediately preceding (2009-2011) and following (2012-2015) the full adoption of IFRS in Malaysia.

In the following tables, test results provide descriptive statistics of pre-post IFRS full adoption for each period that can be seen in Tables 4 and 5. These tables provide a comparison of DACC and other variables during the period of pre-post adoption of IFRS.

Table 4 reports descriptive statistics of pre-IFRS adoption for total observation (N) in 243 firms over a three-year period, 2009– 2011. The maximum value of DACC is 0.6974, while the mean is -0.22375. However, Table 5, which reports descriptive statistics for post-IFRS adoption with a total observation (N) of 324 firms over a four-years period 2012– 2015, indicates that the maximum value of DACC is 0.6239, while the mean is -0.2037. If we compare the maximum and mean values of DACC, before (max= 0.6974 & mean= -0.22375) and after (max= 0.6239 & mean= -0.2037) IFRS full adoption, we can conclude that DACC firms during post-IFRS adoption are smaller than the DACC firms before adoption of IFRS. This indicates that after the adoption of IFRS the EM practices are lessened. The result of this study is consistent with Barth et al (2008), which stated that companies adopting IFRS have less EM practices and thus provide more value relevance—all qualified as higher quality financial statements.

Table 4: Descriptive Statistics Pre-IFRS full adoption (Years of 2009-2011)

Descriptive Statistics					
	N	**Min**	**Max**	**Mean**	**Std. Dev**
ACIND	243	2	5	2.95	0.824
ACFEX	243	1	4	2.19	0.845
ACMEET	243	3	10	4.72	1.397
ACSIZE	243	3	6	3.50	0.700
AQ	243	0	1	0.63	0.436
BSIZE	243	4	14	8.14	2.375
FIRMLEV	243	2	6156	2137.60	1660.46
DACC	243	-1.2562	0.6974	-0.22375	0.23861
Valid N (listwise)	243				

Notes: The table reports summary statistics (minimum, maximum, mean, standard deviations and numbers of observations) for a number of variables for our sample firm-year observations using data for a period immediately preceding IFRS full adoption (2009-2011)

Table 5: Descriptive Statistics Post-IFRS full adoption (Years of 2012-2015)

Descriptive Statistics					
	N	**Min**	**Max**	**Mean**	**Std. Dev**
ACIND	324	2	5	2.88	0.787
ACFEX	324	1	5	2.69	0.827
ACMEET	324	4	16	5.52	1.708
ACSIZE	324	3	8	3.49	0.732
AQ	324	0	1	0.72	0.449
BSIZE	324	2	6302	2091.00	1647.13
FIRMLEV	324	4	16	8.28	2.400
DACC	324	-1.0110	0.6239	-0.2037	0.2459
Valid N (listwise)	324				

Notes: The table reports summary statistics (minimum, maximum, mean, standard deviations and numbers of observations) for a number of variables for our sample firm-year observations using data for a period following or post-IFRS full adoption (2012-2015).

6.2. Hypotheses Testing

The empirical findings shown in Table 6 describe the relationship between AC (ACIND, ACMEET, ACFEX, ACSIZE) and EM both during pre-post IFRS full adoption in Malaysia. Table 6 presents a significant increase in sig P-Value, in which pre-IFRS full adoption is 0.001 and post-IFRS full adoption is 0.000 at 1% level significance. Thus, the results also indicate that the R2 is increasing during the post-IFRS full adoption, with a 4 percent increase to 38 percent. The result of the hypothesis testing (H1 & H2) provides evidence that during post-IFRS full adoption, ACFEX, FIRMLEV and BSIZE are statistically significant (upwards) and ACMEET is significantly at 5% level. It means that ACFEX is significantly effective to EM, which is consistent with Hasan's (2017) study.

Table 6: The Relationship between AC and EM during Pre-Post IFRS full adoption

Pre-Post IFRS full adoption Equation:

DACC i, t = α 0 + α1 ACIND + α2 ACFEX + α3 ACMEET + α4 ACSIZE + α5 BRDSIZE + α6 FRMLEV + ε

Variables	*Exp. Sign*	*IFRS*			
		Pre-IFRS Adoption		***Post-IFRS Adoption***	
		T	*Sig (P-Value)*	*t*	*Sig (P-Value)*
Constanta		-1.286	(0.165)	-1.426	(0.367)
ACIND	-	-0.419	(0.676)	-0.268	(0.432)
ACFEX	-	-2.265	(0.032) **	-2.635	(0.011) **
ACMEET	-	-1.532	(0.121)	-2.316	(0.028) **
ACSIZE	-	-0.437	(0.663)	-0.187	(0.572)
BSIZE	-/+	-0.682	(0.434)	-2.286	(0.032) **
FIRMLEV	-/+	2.415	(0.021) **	2.429	(0.016) **
N			243		324
R^2			0.340		0.380
Adjusted R^2			0.141		0.193
F-Value (P-Value)		3.678 (0.001) ***		5.165 (0.000) ***	

Dependent Variable: DACC

*, **, ***Statistical significance at the 10, 5 and 1 per cent level, respectively

Notes: Estimation results using multiple regression Ordinary Least Squares (OLS) for a period immediately preceding or pre-IFRS full adoption (2009-2011) and following or post-IFRS full adoption (2012-2015) the adoption of IFRS. The dependent variable is Earnings Management (EM) which is proxied by discretionary accruals (DACC) and estimated under the Modified Jones model (Dechow,1995). The Independent variables in this study including Audit Committee Independent (ACIND) measured by Total number of independent board members on the Audit Committee, Audit Committee Financial Expertise (ACFEX) measured by Total number of AC members with financial and accounting background, Audit Committee Meetings (ACMEET) measured by yearly number of meetings, and Audit Committee Size (ACSIZE) measured by total number of members, Control Variables in this study are Board Directors Size (BRDSIZE) measured by the number of directors on the board and Firm Leverage (FRMLEV) measured by Total long-term debt by total assets at the firm i in year t.

Moreover, according to Table 6 during the pre-IFRS full adoption, ACMEET is not related to EM since it is not significant (P-Value = 0.121 > 0.05). However, during post-IFRS full adoption, ACMEET is shown to be negatively significant with EM. This finding is consistent with Chang and Sun (2009), Lin, et al. (2006), and Xie, et al. (2003), as they argue that the frequency of ACMEETs is related to a decrease in discretionary accrual levels. Previous research judged the frequency of ACMEETs as like a signal of extended diligent practice among the AC members (Klien 2002; Habbash 2010; Habbash, et al. 2013). Meanwhile, neither of ACIND and ACSIZE is significant (P-Value > 0.05). For the control variable, FIRMLEV is significantly related to EM in both periods, and the coefficient is positive as predicted. On the other hand, BSIZE is negatively significant related to EM, but not significant in the pre-IFRS full adoption period. This result is consistent with Hasan (2017).

Most importantly, the current study provides empirical evidence on the effect of AQ as a moderator between AC and EM, in both periods of pre-post IFRS full adoption in Malaysia (H3). Based on the result in Table 7, it has reported a significant negative relationship between ACs and EM both during pre-post IFRS full adoption. From Table 7, it is also reported that the effect of AQ as a moderator between AC and EM, increases the relationship as shown in the R2 from 0.392 to 0.412 during post-IFRS full adoption with a P-Value (0.000), as predicted. However, the relationship was found more strongly significant P-Value, as ACFEX (0.001) is significant at 1% level significance compared to ACFEX (0.012) at 5 % level, ACMEET (0.011) is significant at 5% level significance, and AQ (0.011) is significant at 5% level significance, when AQ as a moderator during the post-IFRS full adoption period.

Table 7: AQ as moderator between AC and EM during Pre-Post IFRS full adoption

Pre-Post IFRS full adoption Equation:

$$DACC\ i,t = \alpha\ 0 + \alpha 1\ ACIND + \alpha 2\ ACFEX + \alpha 3\ ACMEET + \alpha 4\ ACSIZE + \alpha 5\ AQ + \alpha 6 ACIND*AQ + \alpha 7\ ACFEX*AQ + \alpha 8 ACMEET*AQ + \alpha 9\ ACSIZE*AQ + \alpha 10 BRDSIZE + \alpha 11\ FRMLEV + \varepsilon$$

Variables	*Exp. Sign*	*IFRS*			
		Pre-IFRS Adoption		***Post-IFRS Adoption***	
		T	*Sig (P-Value)*	*t*	*Sig (P-Value)*
Constanta		-2.434	(0.025)	-2.978	(0.017)
ACIND	-	-0.519	(0.321)	-0.768	(0.272)
ACFEX	-	-2.446	(0.012) **	-3.135	(0.001) ***
ACMEET	-	-1.734	(0.081)	-2.816	(0.011) **
ACSIZE	-	-0.437	(0.663)	-0.187	(0.465)
AQ	-	-2.267	(0.036) **	-2.968	(0.011) **
ACIND*AQ	-	-0.669	(0.272)	-0.943	(0.115)
ACFEX*AQ	-	-2.773	(0.010) **	-2.773	(0.010) **
ACMEET*AQ	-	-1.444	(0.097)	-1.975	(0.062)
ACSIZE*AQ		-0.683	(0.554)	-0.866	(0.354)
BSIZE	-/+	-0.962	(0.133)	-1.042	(0.092)
FIRMLEV	-/+	2.615	(0.017) **	2.985	(0.011) **
N			243		324
R^2			0.392		0.412
Adjusted R^2			0.246		0.291
F-Value (P-Value)		5.918 (0.000) ***		7.417 (0.000) ***	

Dependent Variable: DACC

*, **, ***Statistical significance at the 10, 5 and 1 per cent level, respectively

Notes: Estimation results using multiple regression Ordinary Least Squares (OLS) for a period immediately preceding or pre-IFRS full adoption (2009-2011) and following or post-IFRS full adoption (2012-2015) the adoption of IFRS. The dependent variable is Earnings Management which proxied by discretionary accruals (DACC) and estimated under the Modified Jones model (Dechow,1995). The Independent variables in this study including Audit Committee Independent (ACIND) measured by Total number of independent board members on the Audit Committee, Audit Committee Financial Expertise (ACFEX) measured by Total number of AC members with financial and accounting background, Audit Committee Meetings (ACMEET) measured by the yearly number of audit committee meetings, and Audit Committee Size (ACSIZE) measured by

Total number of members on the Audit Committee, Control Variables in this study are Board Directors Size (BRDSIZE) measured by the number of directors on the board and Firm Leverage (FRMLEV) measured by Total long-term debt by total assets at the firm i in year t.

Table 7 shows all the interaction items, that is, ACIND*QA, ACFEX*QA, ACMEET*QA, ACSIZE*QA, during pre-IFRS full adoption having a less significant level as compared against the post-IFRS full adoption period. Meanwhile, only ACFEX*QA is significant with a higher significant value during the post-IFRS full adoption. The interaction ACFEX*QA pre- adoption P-Value is 0.010 and after adoption P-Value is 0.006 significant at 5% level. This result means that the effect of QA as a moderator in the relationship between AC and DACC, in post-IFRS full adoption period there is a better difference value. This finding concurs with previous studies by Kent et al., (2010) and Prawitt et al., (2009), which documented that AQ and EM were negatively significant and implied that the use of Big-4 audit firms is significantly related to a reduction in the level of EM. This result is also consistent with Chua, Cheong and Gould (2012) who stated that the mandatory adoption of IFRS resulted in better accounting quality.

For the other remaining variables (ACIND, ACSIZE, ACMEET and control variable BSIZE), the results were not significant in either period. This finding was in concurrence with Hasan (2017) in the same Malaysian companies and with Al Shetwi et al, (2011), which used Saudi Arabian companies. This study was not consistent with previous studies such as Kent et al., (2010) and Prawitt et al., (2009). The differences may reflect the poor regulatory environment as compared to that found in advanced countries like the USA.

Table 8 summarizes the descriptive statistics of EM for the year of pre-post IFRS full adoption in Malaysia. However, after the adoption of IFRS, the mean is lower and its EM in pre-IFRS full adoption is higher using paired sample t-test. This indicates that Malaysian companies have higher accounting qualities after the adoption period as compared to the period before the adoption of IFRS. After the adoption of IFRS, the results suggest a reduction, but do not eliminate EM. The result is consistent with the findings by Barth, et al (2008), Zhou, et al. (2009), Chua et al.

(2012), Sellami and Slimi (2016) and Wan Abdullah, et al (2017).

Table 8: Descriptive statistics Paired Sample IFRS full adoption

Paired Samples Statistics					
		Mean	N	Std. Dev	Std. Error Mean
Pair	*Pre-IFRS*	-0.223758	81	0.188261	0.020917
	Post-IFRS	-0.203794	81	0.197060	0.021895

Notes: The table reports a summary of descriptive statistics (mean, standard deviations, standard error mean and numbers of observations) for a number of earnings management variables for our sample firm-year observations using data for pre-IFRS full adoption (2009-2011) and post-IFRS full adoption (2012-2015)

Regarding the test of H4, Table 9 presents the result of a Paired Sample t-test of EM for the period before and after the adoption of IFRS in Malaysia. The results show that there was no significant difference (sig. 0.603 > 0.05) between the levels of EM pre-post adoption of IFRS in Malaysia at 5% level significance. Under the expectation that IFRS full adoption should lead to improvements in accounting quality, this result reveals that pre-post IFRS full adoption in Malaysian companies still tend towards EM practices. This finding provides empirical evidence that EM practices continue albeit under different forms.

Table 9: Paired Sample t-test of Earnings Management Pre-Post IFRS full adoption

Paired Samples Test										
		Paired Differences					t	Df	Sig (2-tailed)
		Mean	Std. Dev	Std. Error Mean	95% Confidence Int. of the Differ				
					Lower	Upper			
Pair 1	*Pre-IFRS*	-0.22375	0.17305	0.01922	-0.0282	0.04830	0.522	80	**0.603**
	Post-IFRS	-0.20379							

Notes: Result of paired sample t-test earnings management variable using significant at 5% level. Pair mean earnings management variable pre-IFRS full adoption and post-IFRS full adoption. Sample firm-year observations using data for pre-IFRS full adoption (2009-2011) and post-IFRS full adoption (2012-2015).

Overall, the results for both years suggest that the companies manage income using decreasing accruals. This indicates that Malaysian companies display higher accounting qualities after the full adoption period as compared to the period before the full adoption of IFRS. However, the mean for the year pre-IFRS full adoption is -0.22375 and the mean for the year post-IFRS adoption is -0.20379 (as shown in Table 9).

7. Conclusion:

This study provided empirical evidence of the effect of mandatory IFRS full adoption in Malaysian companies in the relationship between AC and FRQ (EM-DACC proxy). The results of the hypothesis test (see Table 10) provided evidence that in the period of post-IFRS full adoption, ACFEX is statistically significant (upward) and ACMEET is significantly at 5% level. This is consistent with Chang and Sun (2009), Lin et al. (2006), and Xie et al. (2003). Neither ACIND nor ACSIZE is significant at the same time, decreasing in mean DACC pre-post IFRS full adoption. This result is consistent with Chua et al (2012).

Importantly, this study provides empirical evidence for the situation of mandatory IFRS full adoption in Malaysia, finding that the effect of AQ is significantly increased in the relationship between AC (ACFEX, ACMEET and AQ) and FRQ. Furthermore, in the period of post-IFRS full adoption, interaction with AC and AQ (ACIND*AQ, ACFEX*AQ, ACMEET*AQ, ACSIZE*AQ) reveals a difference in values if it is compared against the period of pre-IFRS full adoption. This evidence shows that the interaction is strongly negative in relation to EM and thus it would improve FRQ. However, the mean value of DACC during post-IFRS full adoption is lower than pre-IFRS adoption, indicating less EM, even though there is no difference between both periods in management discretion.

Table 10: Summary Result of Hypothesis Testing

Hypothesis	Sign	*Sig (P-Value)*	Decision
H1 a	**-**	(0.676)	**Rejected**
H1 b	**-**	(0.032) **	**Accepted**
H1 c	**-**	(0.121)	**Rejected**
H1 d	**-**	(0.663)	**Rejected**
H2 a	-	(0.432)	**Rejected**
H2 b	-	(0.011) **	**Accepted**
H2 c	-	(0.028) **	**Accepted**
H2 d	-	(0.572)	**Rejected**
H3	-	(0.000) ***	**Accepted**
H4	-	(0.603)	**Rejected**

This indicates that Malaysian companies have higher accounting qualities after fully adopting IFRS. Further, AQ as a moderator would limit the DACC while the role of AC is effective. Also, this study contributes to the body of literature on the effect of IFRS full adoption in a situation where AQ as a moderator relates to AC and EM.

This finding also has a critical implication for regulatory bodies and policy makers regarding financial reporting practices in Malaysia and in improving the quality of financial reports. Finally, future research could explore other variables, including moderators that could mitigate the relationship between ACs and EM, especially in emerging markets. Future research could also be expanded to all listed companies and be extended for more years of observation.

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الأثر المُعدّل للأربعة الكبار على لجنة التدقيق وإدارة المدخولات: أثناء ما قبل-بعد تبني المعايير الدولية للتقرير المالي في ماليزيا

محمد سالم محمد بعيو[1]

مجدي أحمد فتحي البناني[2]

محمد علي بن عبدالله حامد[3]

ملخص البحث:

تهدف هذه الدراسة إلى فحص الأثر المعتدل لنوعية التدقيق على لجنة التدقيق، ونوعية التقرير المالي خلال مدة ما قبل وبعد التبني الكامل للمعايير الدولية للتقرير المالي. وتفترض أن فعالية لجنة التدقيق في تطوير التقرير المالي يعتمد على المدقق المختار. ويعتمد بناء نموذج الدراسة على قياسات لمتغيرات مستقلة، وتابعة، ومعتدلة، ورقابية، مثل: الاستحقاقات الاختيارية، وعدد مرات الاجتماعات السنوية للجنة التدقيق، ومتغيرات وهمية. قيست نوعية التدقيق بمعرفة هل الشركة اختارت المدقق من أحد الأربعة الكبار أو من غيرها كمؤشر للطلب على النوعية العالية\المنخفضة للتقارير المالية. واعتمدت الدراسة على بيانات عينة مكونة من 567 شركة من الشركات المدرجة في المدة من 2009 إلى 2015م، وفحصت الفروق ذات الدلالة الإحصائية قبل وبعد تبني هذه الشركات للمعايير الدولية للتقرير المالي في إعداد التقارير المالية باستخدام تحليل الانحدار المتعدد واختبار العينة (t-test). أظهرت نتائج الدراسة أن اختيار المدقق من الأربعة الكبار يسهم في زيادة فعالية دور لجنة التدقيق في تحسين نوعية التقرير المالي بشرط تبني هذه الشركات للمعايير الدولية للتقرير المالي. كما أظهرت نتائج الدراسة أن التبني الكامل للمعايير الدولية للتقرير المالي في إعداد التقارير المالية حدَّ من الخيارات الإدارية وإدارة المدخولات في الشركات الماليزية.

الكلمات الدالة: التبني الكامل للمعايير الدولية للتقرير المالي، نوعية التدقيق، لجنة التدقيق، إدارة الأرباح.

(1) الأكاديمية الليبية مصراتة (مصراتة - ليبيا)

drmagdi.e@uaqu.ac.ae

(2) كلية التجارة - جامعة عين شمس (القاهرة - مصر)

(3) كلية بترا لإدارة الأعمال (سردنج - ماليزيا)