CHAPTER ONE

INTRODUCTION

1.1 Introduction.

Timeliness is an important characteristic of the usefulness of the financial information. Malaysian Accounting Standards Board (MASB) through a proposed conceptual framework for the preparation and presentation of financial statement has established that timeliness is part of the qualitative characteristic of a useful financial statement. Paragraph 42, of DP 1of proposed conceptual framework stated that "for information to be relevant it must also be available to decision makers before it loses its capacity to influence their decisions".

In terms of the capital market, timely reporting can contribute to the efficient performance of stock. As the capital market becomes more sophisticated, financial information is only useful when it is distributed quickly and widely. The faster the information is digested by the users the more efficient the capital market will be.

Malaysia is one of the largest emerging capital markets in Southeast Asia region. Its' stock exchange comprises of more than 800 companies listed on the first board and second board. The Malaysian government through its agencies such as Kuala Lumpur Stock Exchange (KLSE) and Securities Commission (SC) has played an important role in developing the capital market. The Asian financial crisis that started in Thailand had raised awareness among the policy maker of how important to sustain a reliable corporate reporting climate in the country. Recently Corporate Governance has been a hot issue that leads to the implementation of several regulations that are meant to upgrade investor
perspective to the Malaysian Corporate communities for example rules restricting directorship of directors of public companies to twenty five directors and the director cannot hold more than 10 listed companies, code on takeovers and mergers, provision relating to disclosure on related party transactions and quarterly reporting.

Annual reports are expected to be user-friendly, informative and timely. With the rapid expansion of the capital market the quality of annual report would become more important and essential as a vehicle of corporate communication towards enhancing investor confidence.

A requirement for quarterly financial reporting was announced on the 11th March 1999 by Kuala Lumpur Stock Exchange. However this requirement is only applicable for the listed enterprises. Responding to the KLSE quarterly financial reporting, MASB then introduced MASB SOP 2 (Interim Financial Reporting). The objective of the statement is to provide guidance on the application of accounting principles to public listed enterprises in the presentation of interim financial statements. The principles presented in the statement are aimed at facilitating compliance with KLSE listing requirements on the Quarterly Reporting of Financial Statements.

According to MASB SOP 2, enterprises are encouraged to make their interim financial statements available within 60 days of the interim period (paragraph 3). Interim financial reporting is not a new thing. It has been introduced by numerous stock exchanges and securities regulators in other countries. In the United States, private companies also tend to report quarterly to their creditors and other financial institutions (American Institute of Certified Public Accountants Database).

Prior to the new listing requirement, listed companies in Malaysia were only required to file their financial statements annually and made them available to the
public within six months after the year end period. With the new requirement associated with the interim reporting, it is expected to reduce the delay in the preparation releasing financial statements.

The purpose of this study is to examine and to measure the impact of the new requirement interim reporting on the timeliness of financial reporting. The requirement regarding the content of interim reporting and final annual reporting are not exactly the same. As noted in paragraph 6, KLSE requires a quarterly financial statements comprising a balance sheet, an income statement and explanatory notes on a consolidated basis. According to MASB SOP 2, interim reporting should provide current data on financial position, results of operations and changes in financial position (paragraph 37). To meet these information needs, an enterprise may publish either a complete set of financial statements or a set of condensed financial statements. On the other hand final annual reports should be presented according to MASB 1, Presentation of Financial Statements. Having quarterly reporting is just fulfilling the first element of timeliness concept that is on the reporting interval. Another element of timeliness is concerned with the delay of the final annual reporting. Both are equally important in order to meet the concept of timeliness. This will be discussed next.

1.2 The importance of Timeliness

Conceptually, timeliness specifies a quality of: (i) being available at sustainable time or (ii) being well-timed (Gregory and Van Horn, 1963). John K Courtis (1976) defines "Timeliness as one of the qualitative objectives of financial statements, requires that the publication of accounting information be as rapid as possible to assure the availability of current information in the hands of investors and other interested parties"

As discussed briefly at the above paragraph, there are two important elements of timeliness: "reporting interval" and reporting delay. The first element of
timeliness refers to the frequency of reporting. According to the American Institute of Certified Public Accountants (AICPA) database, most of the developed countries such as US, Canada, UK, Australia and New Zealand report quarterly as what KLSE requires now. Prior to the new requirement of KLSE listing, listed enterprises in Malaysia announced their financial statement semi-annually.

The second element of timeliness is "reporting delay". It refers to the number of days starting from the financial year end date to the date information is made available to the public. Besides the frequent interim reporting, reducing the reporting delay in releasing financial statement is also crucial.

Another reason why annual reports should be released timely is because of the absent of auditors' opinion in the quarterly reporting whereas the annual reports need to be reviewed by the external auditor before it can be released to the public. MASB SOP 2 does not require the interim reporting to be audited. This raised the issue of certainty on the provision of the information.

The timeliness of reporting influences the dissemination of information to the general public. The more frequent reporting serves the capital market better and faster investment decisions may be made to direct capital to uses that will maximize the overall economic welfare.

Securities Commission in its capital market master plan, recognizes the need to ensure a high standard of financial reporting and continuous disclosure of timely, relevant and accurate information. This is important for Malaysia to achieve its long run economic objective. As stated in the master plan that is to be a highly efficient conduit for the mobilization and allocation of fund.
Timeliness also plays an important role in the situation where the economy is said to be characterized by information asymmetry. It could help mitigate the fundamental adverse selection problem such as insider trading. The longer a company waits to release information to the public, the more likely the information will become known to small and selected group that can be used for trade for its own benefit.

In Malaysia, the 1997 Asian economic crisis has brought a great impact on the awareness to strengthen corporate governance standards among the public listed companies. This involves the reporting aspect of financial information. The government on the advice of the commission has established a high-level finance committee that later submitted a report covering three big areas. One of the areas is the reformation of laws and regulation to strengthen the overall regulatory framework for the public listed companies. The other two areas are concerned with developing a Malaysian Code on Corporate Governance and Training and Education. Among others, the corporate regulations include improving information accuracy and timeliness of disclosure.

History has shown that regulation is needed to protect investors. This study would like to quote Australian Company Law Advisory Committee in its First Interim Report (1970) cited from Whittred (1980) which states: "Undoubtedly one of the most potent weapons available for the protection of investors is the compulsory disclosure of information......"page 5. Depending on the market forces alone fail to control the adverse selection problem. If we look back at the US history, prior to 1933 their markets were relatively unregulated. Only after the 1929 stock market crash and great depression that the SEC became to restructure and strengthen the act. This led to the setting of appropriate standards and regulation .(William R Scott, 1996)
1.3 Regulatory framework on the timeliness.

To ensure the annual report is released on time, a general requirement of timely reporting is imposed by two regulatory sources in Malaysia. There are:
(a) Companies Act 1965
(b) The KLSE listing requirement.

Section 169 sub-section 2 of the Companies Act 1965 requires that the accounts must be presented within six months of the Balance Sheet date. For a new company the annual accounts must be presented not later than 18 months after the incorporation date. The act also states that the accounts must be tabled in every calendar year. After tabling it at the Annual General Meeting (AGM), it is to be lodged with the Registrar of Companies together with the annual return of the company that consists of relevant information about the company. The submission must be made within one month after the presentation at the AGM.

With regard to companies listed on the KLSE, the requirement is more stringent. It covers both elements of timeliness. In March 1999, KLSE has announced listing requirements on the Quarterly Reporting of Financial Statements. The financial statements should consist of a balance sheet, income statement and explanatory notes. The listing requirement requires quarterly reporting to be submitted to the KLSE within 60 days of the interim period end.

On the other part, KLSE is also concerned with the delay in releasing annual report. According to Chapter 9 paragraph 23- KLSE listing requirement, the annual report shall be issued to the listed issuer's shareholders within a period not exceeding 6 months from the close of financial year. Meanwhile the annual audited accounts together with the auditors and directors reports shall be given to the KLSE for the public release within a period not exceeding 4 months from the close of financial year of the companies unless the annual report is issued
within that period. This means that if the company issues the annual report after 4 month of the close of financial year, the company has to provide annual audited accounts within 4 months of the close of financial year. On the other hand if the company issues its annual report within 4 months, it does not have to provide annual audited accounts. This is to encourage information being made available to the public quickly, fairly and widely.

1.4 Problem definition.

The period after the Asian financial crisis has been seen as a period of reconciliation on the Malaysia capital market. In order to make the market attractive and competitive, several new regulations have been introduced. However, regulation without being monitored and coordinated is meaningless.

This study focuses on the effectiveness of the new listing requirement imposed by KLSE. So far as is known no such published research has been carried out in Malaysia. The existing literature mainly focused on the benefits of the interim reporting (example: Susan Tho Lai Mooi (1994) and Annuar, MN and Shamser M (1992). Overseas studies on the timeliness on the other hand mainly focused on the criteria that influence the timeliness for example Dyer and McHugh (1975), Couris (1976), Gilling (1977), Abdulla (1996) and Stephen Owusu-Ansah (2000) and the impact of timeliness to the stock price for example Foster G (1977), Griffin P.A (1977) and Lorek K.S (1979). The criteria mention above refer to company size, profitability, year end period, industry and audit firm.

This study intends to observe the effectiveness of the new measures taken in order to ensure timeliness particularly on the effect of quarterly reporting on the timeliness of final annual report.
1.5 Objective of the research.

The overall purpose of this research is to study the impact of the new quarterly reporting requirement on the timeliness of final annual reporting of the listed companies.

The research intends to cover the following areas:

1) Comparison between timeliness of reporting before the implementation of the quarterly reporting requirement and after.
2) The number of days taken between the balance sheet date and the date KLSE received the full annual report for the public purpose in all the relevant periods. (1997, 1998, 1999 & 2000).

1.6 Scope and limitation.

This study focuses on the companies that are listed in the KLSE which are required to comply with the Quarterly Reporting requirement. The samples chosen cover all industries. Every sector of industries will be included in the samples. The size of the samples is based on the percentage of twenty five percent of the total number of companies listed in the KLSE as at 1997. In 1997, there are 434 companies listed in the first board and 234 companies listed on the second board (KLSE Annual Companies Handbook 1997). Therefore the total companies chose are approximately 170 companies. The period of study covers four years (1997, 1998, 1999 & 2000).

There are three limitations identified in this study. Firstly, this study focuses only on the impact of the new listing requirements that is quarterly reporting
requirement. It is a comparative study between two periods, before and after the quarterly reporting requirement took place. Therefore the existing factors that could influence the reporting delay such as size of the firm, profitability and year end period which are already embedded in the subjects is ignored. The next limitation is the availability of the annual reports for the samples chosen. There are some annual reports missing from the KLSE library and does not available in the KLSE website. This affects the selection methods of the samples. Therefore only the companies which annual reports are available in all relevant periods were chosen into the samples. The last limitation is that the number of companies chosen as the sample in this study might not be large enough to generalize the findings.

1.7 Organization of the study.

The remainder of this study is arranged as follows; Chapter 2 will be looking at the previous literature for the development of theoretical framework. It will also touch on the development of the testable hypothesis. The subsequent chapters will discuss the research methodology and data analysis technique for this study. Chapter 4 reports and discusses the findings. Finally, chapter 5 presents the conclusion and the recommendation for the future study.