



**SEGMENTAL REPORTING IN MALAYSIA:
THE DISCLOSURE AND PERCEIVED
IMPORTANCE**

BY

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ABSTRACT

Segment reporting is not a new issue in the disclosure of corporate annual report, either locally or internationally. However, due to the rapid growth experienced by Malaysian companies as a result of globalization and diversified business activities, segment reporting is gaining importance. Since then, there have been many significant changes in the accounting regulation with regards to segment reporting, and apparently, segment information is very much needed in order to better assist stakeholders in making decisions. Hence, this study aims to identify the extents of segment disclosure of financial and non financial information in the corporate annual reports of Malaysian public listed companies. In addition, there is also the need to identify the perception of various stakeholders regarding the importance of financial and non financial information of segment information and to further identify the factors explaining the extents of segment disclosure based on proprietary cost theory. Data for this study were collected through questionnaire surveys, interviews and companies' annual reports. Four years of annual reports were used from a sample of 93 Malaysian public listed companies' and statistical analysis were conducted. The analysis results show that non financial information are more disclosed than financial information. The results also reveal that the introduction of new regulations in FRS 114 has led companies to produce better disclosures than under MASB 22 or previous regulations. The analysis on stakeholders' perception reveals that there is no significant difference towards the importance of financial information among all stakeholders. Financial analysts were found to perceive non financial information as the most important, followed by the group of managers. Overall, non financial information is considered the most essential to all stakeholders in making decisions. Apparently, no significant relationship was found between all independent variables and financial segment disclosure except for number of segment. For the relationship between control variables and financial segment disclosure, only diffusion and return on asset are significant. In contrast, the relationship between independent variables and control variables with non financial segment disclosure are found to be all insignificant. As for interview sessions, results show that company did not highlight significantly the factors of proprietary cost in preparing the segment information disclosure, even though certain determined factors such as cost consideration and sensitivity lead indirectly toward proprietary cost theory. In conclusion, the term proprietary cost theory is still not well-known among preparers of annual report in Malaysian public listed companies. Overall, this study has provided helpful insights to users, preparers, accounting regulators in segment reporting especially in improving the financial reporting so that it is geared to meet stakeholders' expectations.

خلاصة البحث

مسألة الإبلاغ شريحة ليست جديدة في الكشف عن التقرير السنوي للشركات، سواء محليا أو دوليا. ومع ذلك، فإنه يبدو أن الزيادة في أهمية والعديد من الشركات في ماليزيا في الآونة الأخيرة، شهدت نموا سريعا خلال العولمة وتنويع الأنشطة التجارية. لأن هناك العديد من التغيرات الهامة في تنظيم المحاسبة فيما يتعلق بالتقرير الجزئي، وبالتالي هناك حاجة واضحة للحصول على معلومات الجزئي من أجل مساعدة المستخدمين في اتخاذ قرارات أكثر اطلاعا. هذه المدرسة تهدف إلى تحديد (1) نطاقات الكشف جزئي من المعلومات المالية وغير المالية في التقارير السنوية للشركات في شركات عامة مدرجة في ماليزيا. (2) تصور مختلف أصحاب المصلحة بشأن أهمية المعلومات المالية وغير المالية والكشف عن الجزئي. (3) العوامل التي توضح نطاقات الكشف الجزئي على أساس نظرية تكلفة الملكية. كانت تستخدم بيانات أولية (الاستبيان والمقابلة)، وبيانات الثانوية (التقرير السنوي) لإجراء الدراسة. لاختبار الفرضيات، وعينة من التقرير السنوي 93 الماليزي للشركات عامة مدرجة لمدة أربع سنوات أي عام 2000، 2002، 2004 واختير عام 2006، وإحصاء وصفي كانت تستخدم عينة المتقارنة اختبار ومتعددة نموذج الانحدار. النتائج للنطاقات الكشف هي على النحو التالي. أولا، تبين أن الشركات بالكشف عن المعلومات المالية وغير المالية على حد سواء. ثانيا، أظهرت النتائج أنه بعد الأخذ في اللائحة الجديدة في FRS114 يصبح أفضل من الكشف MASB22 أو الأنظمة السابقة. لاحقا، العثور على نتائج التحليل لإدراك أصحاب المصلحة أنه لا يوجد فرق كبير لأهمية المعلومات المالية بين جميع أصحاب المصلحة. ومع ذلك، ينظر إلى المحللين الماليين أعلى أهمية المعلومات غير المالية التي تتبعها مجموعة من المدير. عموما، تعتبر هذه المعلومات غير المالية الضرورية لجميع الجهات المعنية من أجل إتخاذ القرارات. نتائج الانحدار تبين أن ليست هناك علاقة كبيرة بين جميع المتغيرات المستقلة والإفصاح المالي الجزئي باستثناء عدد من الجزئي. بالنسبة للعلاقة بين المتغيرات المالية و مراقبة الإفصاح عن الجزئي، ونشرها فقط، والعائد على الأصول الكبيرة. من ناحية أخرى، فإن العلاقة بين المتغيرات المستقلة والمتغيرات التحكم مع عدم الكشف عن الجزئي المالية ضئيلة. باختصار، فإنه يدل على أن ليس هناك نظرية تكلفة الملكية تنفيذا كاملا في ماليزيا. وجدت النتائج من جلسة مقابلة أنه في الواقع، شركة ماليزية تنفذ بالفعل نظرية تكلفة الملكية على الرغم من أنها لا تعبر بشكل مباشر. لكنه يظهر أيضا أن معد التقرير السنوي في شركة عامة مدرجة في ماليزيا لا تزال غير مدركة للنظرية تكلفة الملكية الأجل. وأخيرا، فإن النتائج التي توصلت إليها الدراسة تقدم بعض الأفكار المفيدة للمستخدمين، معدي، والمنظمين وواضعي السياسات المحاسبية في الممارسة الحالية للشركات وخصوصا الجزئي المتعلق بالتقرير في تحسين تقديم التقارير في المستقبل إلى حد أنه قد تأتي أقرب إلى تلبية توقعات أصحاب المصلحة.

APPROVAL PAGE

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DECLARATION

I hereby declare that this dissertation is the result of my own investigations, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degree at IIUM or other institutions.

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بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

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LIST OF ABBREVIATIONS

AAS 16	Auditing and Assurance Standard 16
ACT	Accountants
ACTCOMP	Accounting complexities
AGE	Listing status age
AICPA	American Institute of Certified Public Accountants
ASC 1990	American Standard Committee 1990
CFO	Chief Financial Officer
CODM	Chief Operating Decision Maker
CORR	Correspondence between segment and identifiable subsidiary
e.g.	For example
DIFF	Ownership Diffusion
DUMMYIND	Dummy industry
DUMMYIND- T	Dummy industry trading
DUMMYIND-NT	Dummy industry non trading
ED 8	Explosure Draft 8
EPS	Earning per share
et al.	(<i>et alia</i>): and others
FA	Financial Analysts
FRS 114	Financial Reporting Standards 114
FRS 134	Financial Reporting Standards 134
Gap-F	Financial Gap
Gap-NF	Non Financial Gap
GLC	Government Link Company
GRO	Growth rate
IAS 14	International Accounting Standards No.14
IAS 14R	International Accounting Standards 14 Revised
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
i.e.	That is
IFRS 8	International Financial Reporting Standard 8
IUM	International Islamic University Malaysia
KLSE	Kuala Lumpur Stock Exchange
LEV	Financial leverage
LOB	Line of Business
MACPA	Malaysian Association of Certified Public Accountants
MASB	Malaysian Accounting Standards Board
MASB 22	Malaysian Accounting Standards Board 22
MASBED 22	Malaysian Accounting Standards Board Exposure Draft 22

MBA	Master of Business and Administration
MGR	Managers
MIA	Malaysian Institute of Accountants
NUMSEG	Number of segment
NYSE	New York Stock Exchange
ODV	Optimised Deprival Valuation
OFR	Operating and financial review
ROA	Return on asset
ROAxLOSS	Return on assets multiple with loss
SEC	Securities and Exchange Commission
SFAS 14	Statement of Financial Accounting Standards No.14
SFAS 131	Statement of Financial Accounting Standards No.131
Sig.	Significant
SIZE	Size of companies
SPSS	Statistic Packages for Social Science
SSAP 25	Standard Accounting Practice No.25
UiTM	Universiti Teknologi Mara
U.K.	United Kingdom
UKM	Universiti Kebangsaan Malaysia
U.S.	United States of America
UTM	Universiti Teknologi Malaysia
UUM	Universiti Utara Malaysia
U.S.	United States of America
U.S.GAAP	United States of America Generally Accepted Accounting Principles
VIF	Variance Inflation Factor

CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF STUDY

Segment reporting has become an important financial reporting issue surrounding the corporate sectors globally due to growing popularity of conglomerate type businesses. In recent years, companies throughout the world have diversified their business enterprises with increasing complexity in their activities. This diversification of activities includes the process of venturing business in different geographical areas (Talha, Sallehuddin and Mohammad, 2008). When a large company conducts its operations that represent distinct products or market segments, it becomes increasingly difficult to analyze the effect of these activities on past performance and their likely effect on future performance of the company (Benjamin, Muthaiyah, Marathamutu and Murugiah, 2010). Similarly, in Malaysia, companies experienced rapid growth through globalization and diversification of business activities. Within this context, the profitability, risks and opportunity for growth and future prospects of such companies may differ substantially among different industries and different geographical locations (Kevin and Mazlina, 2001). In other words, companies nowadays have complex operations consisting a number of activities in a variety of locations with different profitability potential, risks, rates of return and growth opportunities. The segments may vary significantly in terms of profitability, risks and returns (Herrmann and Thomas, 1996).

The last ten years have seen remarkable changes in the development of accounting standards on segment reporting. In 2002, Malaysian Accounting Standard Board (MASB) issued MASB 22, which has made significant reference to IAS 14 in

an effort to converge with the International Accounting Standards. The latest changes in the rules for segment reporting came with the issuance of Financial Reporting Standard 8 (FRS 8) which became effective for accounting period beginning 1 January 2009.

Although FRS 8 has changed the concept of segments to become operating segments, the importance of products' diversifications and various locations of company's operations are still very much considered. For example the requirements of FRS 8 still recommends entity-wide disclosures which includes disclosures of information related to geographical segments. In addition, there is a growing concern on the availability of segment information as required by FRS 8 since the standard was just recently issued. In view of the importance of segment reporting, this study examines this issue based on FRS 114.

In FRS 114, Segment Reporting is defined as information relating to the enterprise's different types of products and services and its operations in different geographical areas. Radebaugh and Gray (2002) defined segment reporting as the counterpoint to consolidated information involving the disaggregation of the consolidated financial statements.

Generally, companies in Malaysia are required to disclose segment information based on FRS 114 Segment Reporting (originally known as International Accounting Standard 14 [IAS 14]) for the periods beginning 1 January 2002. Under FRS 114, two-tier segmentation with either business segment or geographical segment as the primary basis of segment reporting and the other as its secondary basis. Primary segment required full disclosure, while partial disclosure is required for secondary segment. FRS 114 requires consistent use of accounting policies across segments and standardized measure of segment results across companies. By electing to adopt FRS

114 prior to its effective date, companies voluntarily disclose more information especially for the primary basis of segment reporting since they have to provide additional disclosures (Nordin, Noriah and Asma, 2005).

However, when the original IAS 14 was first issued in 1985, many diversified companies listed in Bursa Malaysia (formerly known as Kuala Lumpur Stock Exchange) ignored it and they did not disclose segment information (Tan, 2001). The low compliance rate for segment disclosure according to Tan (2001) could be due to the following reasons; (1) the lack of readability of management accountants to segregate the data into segments in accordance with IAS 14, (2) the companies' perception that the costs of gathering such data outweigh the benefits of disclosure, (3) there was difficulty in the identification and aggregation of operations in segments and in the allocation of some common items to the appropriate segments, (4) the companies that were reporting segment disclosure were not aware of the advantages and benefits of such disclosure and finally, (5) segment information was considered as trade secret by management. Although IAS 14 Reporting Financial Information by segment has been operational in Malaysia since 1987, companies tend not to disclose such information for many reasons (Kevin and Mazlina, 2001).

Even so, as revealed by some previous literature such as Talha et al. (2006), the benefits that could be derived from segment information exceed the above limitations. Prior study demonstrated that segment reporting improves forecasting ability and stock market investors particularly found the information useful (Roberts, 2000). Theoretically, segment information should enable the financial analysts and investors to analyze more precisely the component parts of the total firm and thereby evaluate the firm's stock and assess its financial prospects on a more rational basis (Tan and Ngan, 1991). In the study, it was highlighted that segment financial information

should be able to serve the purpose of an increased potential for successful investment decisions by the stakeholders.

1.2 RESEARCH ISSUES AND RESEARCH QUESTIONS

This study covers three main issues. The first focuses on the extent of segment disclosure of financial and non financial information. In addition the implementation of FRS 114 for pre and post period due to the requirement of the new standard which was applicable in 2002 for all public listed companies will also be covered. Secondly, the issue is on the perception of the importance of financial and non financial segment information by various stakeholders. Finally, the issue on the factors explaining the extent of segments' disclosure based on proprietary cost theory which are competitiveness, accounting complexities and loss. As such, these have led to six research questions. Table 1.1 summarizes the research issues and research questions for this study.

Table 1.1
Research issues and research questions of the study

Research Issues	Research Questions
1. The issue of the extent of segment disclosure information and the implementation of FRS 114 for pre and post period due to the requirement of the new standard which was applicable in 2002 for all public listed companies.	<p>RQ1: What is the extent of financial and non financial segment information disclosed in the corporate annual reports of Malaysian public listed companies?</p> <p>RQ2: Is there any difference in the extent of segment disclosure of financial and non financial information for pre and post FRS 114 period?</p>
2. The issue of the perception on the importance of financial and non financial segment information by the various stakeholders.	RQ3: How do various stakeholders view the importance of financial and non financial segment information in corporate annual report of Malaysian public listed companies?
3. The issue on factors explaining the extents of segments disclosure	<p>RQ4: What are the factors explaining the extent of segment disclosure?</p> <p>RQ4(i): Is the competitive disadvantage factor explain the extent of segment information disclosure?</p> <p>RQ4(ii): Is the accounting complexities factor explain the extent of segment information disclosure?</p> <p>RQ4(iii): Is the loss factor explain the extent of segment information disclosure?</p>

1.3 RESEARCH OBJECTIVES

Based on the discussions in the previous section, this study is conducted to examine the extent of segment disclosure of financial and non financial information in corporate annual report of Malaysian public companies. The inclusion of non financial information is added as there were evidence on the increasing importance of non financial information for decision making purposes, Amir and Lev (1996). The introduction of FRS 114 as an effort by MASB to converge with the IFRS might has influence Malaysian companies, particularly those which are listed in Bursa Malaysia to disclose more segment information.

Next, the study identifies various stakeholders' perceptions on the importance of segment disclosure in the corporate annual report of Malaysian public listed companies and fill the gap of the segmental disclosure research in Malaysia since there was no study focusing on this issue. Although segment information are directly related to specialized stakeholders such as financial analysts, the increasing use of stakeholder theory did raise the importance of information in the annual report to other groups of stakeholders¹. Annual report is the most comprehensive document available to the public and is therefore the 'main disclosure vehicle' (Marston and Shrives, 1991). In addition, according to Parker (1982), annual report is important and it was considered a mass communication medium. However, Hooks et al. (2002) highlighted that although annual report is not the only source of information about the performance of company, it is considered to be an influential source due to its wide coverage and availability. Thus, this leads to the second objective of the research.

¹ Kelvin and Mazlina (2001) provided empirical evidence on the extent of compliance of segment disclosure as required by IAS14. Talha et.al. (2007) examined the quality of segment disclosure by Malaysian Listed Companies

The studies of disclosure information is well documented in the literature, however most of them covered disclosure in general. In this study, segment disclosure and factors explaining segment reporting from the proprietary costs perspective are being examined. Previous studies such as Verrechia (1983;1990), Wagenhofers (1990), Sanders, Alexander and Clark (1999) and Prencipe (2004) have highlighted that disaggregation information into various business and geographical segments involve high proprietary costs on the part of business entity. As such, this study has selected a few variables to be a proxy for proprietary costs in explaining segment reporting.

To simplify the above, there are three objectives that the researcher has formed. They are:

- a) To examine the extent of segments' financial and non financial information disclosure during the pre and post-implementation period of FRS 114.
- b) To examine the perceptions of stakeholders on the importance of segments' financial and non financial information.
- c) To examine the factors explaining the extents of segments' disclosure based on the Proprietary Cost theory.

1.4 MOTIVATION AND SIGNIFICANCE OF THE STUDY

Due to the growing and rapid changes in business technology and economy, businesses and corporations began to diversify their business operations into multi-operational and multinational enterprises. The main objective of diversification is to spread risks and to take advantage the opportunities in other markets. With the robust diversification and globalization, it is obvious that the preparation of consolidated

financial statements alone could no longer represent the overall view of financial information precisely and correctly to the users of financial statements. This is due to the different growth rates, profitability and risks among the segments in a diversified operations and companies (Tan and Ngan, 1991). To some extent, there is a lack of correspondence between the financial statement of the reporting entity and the nature of the company's activities, thus requiring the need for disaggregated information in segment reports (Radebaugh and Gray, 2002).

According to Kevin and Mazlina (2001) another aspect that adds to the complexities of the operations is the merger and the acquisition activities of a wide variety of business operations. Due to this, users of the financial statements face difficulties in evaluating predicting future activities of the corporation based on consolidated figures of the income statement, balance sheet and owners' equity statement.

Series of the discussions among accounting standard setters [Refer to Statement of Financial Accounting Standard 14 (SFAS 14) (1976); Standard Accounting Practice 25 (SSAP 25) (1990), International Accounting Standard 14 (IAS 14) (1981), IAS 14 Revised (1997)] and empirical studies (Kochanek, 1974; Collins, 1976; Tan and Ngan, 1991; Kevin and Mazlina, 2001; Street and Nichols, 2002; Kinsey and Meek, 2004 ; ² Talha et al. 2007; Talha et al. 2008) have been done in the area of segment reporting specifically focusing on the relationship between the extent of segment disclosure with firm characteristic, segment reporting and its effects on security prices, compliance rate of segment reporting, analysis of the impact of the

² Talha et al. (2007, 2008) did not capture and exercise pre and post result of FRS 114