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CORPORATE GOVERNANCE MECHANISMS AND ACCRETIVE SHARE BUYBACK TO MEET OR BEAT EARNINGS PER SHARE FORECAST

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ABSTRACT

This study examines the Malaysian accretive share buybacks firms from year 2001 to 2008 to determine the relationship between the corporate governance mechanisms and accretive share buybacks, the earnings management device to meet or beat earnings per share (EPS) forecast. The regression results of this study reports the significant effect on the relationship between corporate governance and accretive share buyback. Basically, there is positive effect on the relationship between the board independence, CEO duality and board size with the accretive share buyback to meet or beat EPS forecast (MBEF). Multiple directorships and managerial ownership documents a negative relationship with accretive share buyback to MBEF. However, this study identified insignificant relationship between board meetings and accretive share buyback. Using the accretive share buyback as an earnings management proxy is a new contribution to determine the roles of corporate governance on accretive share buyback to MBEF rather a common study on accruals manipulations and corporate governance mechanisms.

Keywords: Accretive Share Buyback; Corporate Governance; Earnings Management; Earnings per Share.

1. INTRODUCTION

Earnings are important information in the financial report for analyst, investors, senior executives and board of directors (Degeorge, Patel & Zeckhauser, 1999). Among the various earnings metrics to measure firm performance, earnings per share (EPS) are well-known and essential tool to measure firm performance (Graham, Harvey & Rajgopal, 2005; Seetharaman & Raj, 2011). Investors need a threshold or benchmark to measure the earnings performance as to evaluate firm's financial success and also to compensate the managers. Degeorge et al. (1999) developed three thresholds as follows: (1) to report quarterly profits, (2) to achieve

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quarterly earnings increases as previous year quarterly period, and (3) to achieve quarterly earnings surprises (whether or not actual EPS meets or beats earnings forecast predicted by analysts). According to Brown and Caylor (2005) after mid-1990s, among the three thresholds, achieving earnings surprises (meet or beat EPS forecast – MBEF) is the most salient thresholds due to investors realization on the importance of achieving earnings forecast (positive earnings surprises- MBEF) as it put forward media attention and precision in analyst forecasting. Obviously, meeting or beating earnings forecast (MBEF) is an anchor of today's corporate culture, of being able to boost share prices, maximizing management's credibility and avoiding litigation cost that could trigger from negative earnings surprises (Bartov, Givoly & Hayn, 2002). In general, firms achieve earnings threshold either through business success with good financial performance or through earnings management. It is manifested that, due to business pressure, managers practice earnings management to meet or beat EPS forecast (MBEF). Firms commonly involve in accruals manipulation (indirect impact to cash flows) and real activities manipulation (transactions that gives direct impact to cash flows) as an earnings management proxies to adjust the financial reports. Among the two proxies, real activities manipulation is difficult to detect as it proceeds like an ordinary business transactions in general. Hribar, Jenkins and Johnson (2006) reported that firms used accretive share buyback (real activity manipulation) as the earnings management device to meet or beat EPS forecast. Accretive share buyback is an earnings management tool that can increase post-buyback EPS by a minimum of one cent. Earnings management is a short-term focused that do not contribute to firm value (Roychowdhury, 2006). Further, existence of earnings management activities indicates a flaw in corporate governance practices in the firm (Graham et al., 2005). Because corporate governance is a symbol of good principles and best practices of a firm to protect the shareholders rights and not to mislead shareholders through earnings management practices. Further, an ineffective board monitoring mechanism is detrimental to a firm (Rahman & Ali, 2006). Therefore, strong corporate governance is a remedy to decrease earnings management activities in firms. This study investigates the nature of relationship between the corporate governance mechanisms and accretive share buyback to MBEF. The accretive share buyback to MBEF refers to the usage of accretive share buyback to meet or beat the EPS forecast. Malaysian earnings management studies commonly use accruals manipulation as the earnings management proxy to investigate the relationship between earnings management and corporate governance mechanisms. Therefore, this is a good platform to study on corporate governance mechanisms and the accretive share buyback as the earnings management proxy. This study contributes to the body of knowledge on role of corporate governance mechanisms and accretive share buyback the earnings management device to MBEF.

2. THEORETICAL ASSUMPTIONS OF PRIOR RESEARCH

In Malaysia share buyback is a corporate payout policy where listed firms are allowed to buy back their firm shares under the open market buyback program. The Corporate Law Reform Committee introduced Section 67A, Companies Act, 1965 which allows the solvent Malaysian Public Listed Companies to purchase own shares with the approval of the shareholders not more than 10% of the issued and paid up share capital through Malaysian stock exchange. In Malaysia, share buyback activity has shown a remarkable growth for more than a decade. There are numerous reasons for share buyback activities and commonly it is believed to increase and protects share prices. However, Hribar et al. (2006) finding on United States firms engaged in accretive share buyback as the earnings management device to MBEF, reveals a macro-level information specifically to the corporate world and academics that share buyback can be also used as an earnings management tool to MBEF.

Earnings management occurs when managers use judgment in the financial reporting and in structuring transactions to alter the financial reports to either mislead some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depended to the reported accounting numbers (Healy & Wahlen, 1999, p. 368). Earnings management is a game between investors and managers. Managers engage in earnings management to mask true firm performance as a remedy to avoid investors' disciplinary action (Leuz, Nanda & Wysocki, 2003). Consistently, Chandren, Ahmad and Ali (2015) identified that investors' reward positive share prices to firms for delivering positive earnings surprises news through earnings management. Thus, market reacts positively to positive earnings surprises announcement. Due to this, firms involve in earnings management to meet or beat the EPS forecast (positive earnings surprises) to avoid investors disciplinary action (Chandren et al., 2015).

Separation between ownership and control, increases manager entrenchment level to involve in earnings management by manipulating firm's financial report for their own benefits. This manager's action reduces investors' trust in financial information (Gulzar & Wang, 2011). Therefore, firms need an effective corporate governance to protect the investors' right by controlling the firms' earnings management activities (Gulzar & Wang, 2011). Firms need strong and effective corporate governance mechanisms to reduce earnings management, as to protect the rights of the investors (Rahman & Ali, 2006). Effective corporate governance is important to strife earnings management activities either by accruals manipulation or by real activities manipulation. Good corporate governance requires providing proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders by facilitating effective monitoring (OECD, 2003).

In Malaysia the corporate governance practices came into focus after the Asian Financial Crisis 1997 (Susela, 2003). Malaysian Code of Corporate Governance (MCCG) Code issued in 1999 mainly focuses on corporate governance principles and practices on board of directors, shareholders, accountability and audit. In order to achieve a great efficiency in governance framework, this Code sets out best practices guidelines on structures and processes. After the revamp of Bursa Malaysia Listing requirements in 2001, the Code became effective to listed companies. In 2007, MCCG Code is revised with the aim to strengthen the roles and responsibilities of the Board of Directors. This is to ensure they can discharge their duties effectively (SC, 2007). The Capital Market Masterplan 2 (CMP2) is launched in April 2011 to expand the role of the capital market in invigorating national economic growth as a part of the Malaysia's transformation plans to a developed economy by 2020. Strengthening corporate governance therefore represents one of the key thrusts to reinforce investors trust and confidence in the Malaysian capital market. This Corporate Governance Blueprint represents one of the first deliverables of CMP2. This Blueprint is premised on the paradigm that boards of companies occupy a central role as agents for shareholders, both retail and institutional, within the corporate governance ecosystem. This action plan is launched by Securities Commission in 8 July 2011, the Corporate Governance Blueprint 2011 is known as Malaysian Code of Corporate Governance (MCCG 2012). All listed firms in Malaysia are urged to report on their compliance on MCCG 2012 principles and recommendations in the 2012 annual reports.

The Bursa Malaysia's Listing Requirement states that the listed firms' board of directors must propose the idea of share buyback to the shareholders through circulars. These circulars are used for the approval of the shareholders for the share buyback activities. The board of directors is the responsible monitoring mechanism to monitor the actions of the managers for the interest of the investors (Fama & Jensen, 1983). Thus, this study will focused on the board of directors characteristics as the corporate governance (CG) mechanism to identify the nature of relationship between CG mechanisms and the accretive share buyback. This study adopt the five main board characteristics as used in Saleh, Iskandar and Rahmat (2005) study refers to board independence, CEO duality, board size, multiple directorships and managerial ownership as the component of principles and best practices of effective governance. Further, board meeting is also an important corporate governance mechanism, thus board meeting is included as the one of the corporate governance variable for this study.

3. DEVELOPMENT OF HYPOTHESIS

3.1. Board Independence

Under the Bursa Malaysia Listing Requirement, the public listed companies required to have sufficient number of outside or non-executive directors to protect the interest of investors (Ponnu, 2008). Malaysian Code on Corporate Governance requires Malaysian public listed firms to have at least one-third of the board members to be independent and non-executive directors.

According to Rahman and Ali (2006), more board independence better the monitoring skills and the authors predicted negative relationship between board independence and earnings management. However, the results of Rahman and Ali (2006) and also Hashim and Suppiah (2008) found no significant relationship exist between board independence and earnings management. The agency theory delineates the fact that the more independent directors dominate the board, the greater will be the board's monitoring and controlling the management's opportunistic behavior and expropriation of firm resources (Jensen & Meckling, 1976; Brickley & James, 1987). Consistently, Johari, Saleh and Hassan (2008) found negative relationship between board independence and earnings management which is in line with agency theory. In addition, the authors reported that more board independence results in greater board monitoring mechanism that reduces firm's earnings management activities. Further, Saleh et al. (2005) identified that internal corporate governance mechanism improves with the existence of more independent board. This develops the hypothesis;

H1: There is a negative relationship between board independence and accretive share buyback to MBEF.

3.2. CEO Duality

CEO duality refers to a situation where Chairman is also the CEO of a firm. Malaysian Code on Corporate Governance (MCCG) recommends Malaysian public listed firms to have distinct and separate roles for Chairman and CEO for better balance of power and avoidance of conflict of interest (Ponnu, 2008). Further, Ponnu (2008) said that to promote fair judgment and reasonable concern firm's best practice, no single person in the board allowed controlling other board members in decision making process. The separation of CEO duality is not enforced under MCCG but it is encouraged that the two positions to be separated (Saleh et al., 2005). For firms with CEO duality, MCCG seek for transparency in information for public, concerning to the elements of independent for the two positions as a measure to promote strong governance (Ponnu, 2008).

Johari et al. (2008) highlighted that CEO duality decreases the board monitoring strength. It creates a question "who watches the firm" (Abdullah, 2004). Moreover, Chairman's roles are to chair the board meeting and involve in senior management appointment process and deciding their compensation benefits (Beasley & Sailterio, 2001). Further, if the CEO is also the Chairman, the concentration of power rest with one person which reduces effectiveness of corporate monitoring. The separation of these two positions will be advantage to strengthen the board monitoring (Johari et al., 2008). In line with this, Saleh et al. (2005) and Nahandi, Baghbani and Bolouri (2011) found positive relationships between CEO duality and earnings management. This develops the next hypothesis;

H2: There is a positive relationship between CEO duality and accretive share buyback to MBEF.

3.3. Board Size

Malaysian Codes on Corporate Governance (MCCG) do not regularize board size limit to the listed firms. These listed firms can set their board size as long as the size of boards is able to manage the corporation. Saleh et al. (2005) found that large board is able to minimize earnings management activities. But contrasting opinion from Yermack (1996) that compared to larger board, smaller board size monitors the managers effectively. In sum, smaller boards are active monitors. Similarly, a study conducted by Rahman and Ali (2006) identified that board size is positively related to earnings management. This is because, large board size failed to monitor managers to mitigate earnings management activities (Rahman & Ali, 2006). Thus the next hypothesis is developed;

H3: There is a positive relationship between board size and accretive share buyback to MBEF.

3.4. Board Meetings

Earnings management activities do not signify the true performance of the firm, which influence the shareholders and investors to make inaccurate judgments about the firm. Therefore, board monitoring is essential in decreasing the occurrence of earnings management activities (Gulzar & Wang, 2011). Xie, Davidson and Dadalt (2003) reported that earnings management and board meetings are negatively associated, thus, the more the board meetings the lesser the firms involvement in earnings management activities. In addition from these findings, Bursa Malaysia Listing Requirement set a compulsory standard requirement for all listed companies to disclose in their annual report the number of board meetings conducted for the financial year. Beside this, Gulzar and Wang (2011) found that frequent board meetings heighten the board activeness in monitoring the management activities. Therefore, the next hypothesis is developed;

H4: There is a negative relationship between board meetings and accretive share buyback to MBEF.

3.5. Multiple Directorships

Multiple directorships means holding director position for more than one board (Haniffa & Hudaib, 2006). Practice Note 13 (PN13) issued by Bursa Malaysia in year 2002 allows a maximum number of ten directorships for listed firms and fifteen in private limited firms. Director of the firms with multiple directorships are good monitors that gives positive impact to firm's financial reporting quality (Hashim & Rahman, 2011). As matter of fact, these directors attain monitoring skills (Hashim & Rahman, 2011) from other organization, are able to detect firm's earnings management activities (Saleh et al., 2005). Consistently, Saleh et al. (2005) identified that multiple directorships and earnings management are negatively related. The authors reported that the negative relationship between the earnings management and multiple directorships is due to the gain of experience obtained through directorships in other firms. This shows that earnings management activities are lower for firms with multiple directorships. This develops the next hypothesis;

H5: There is a negative relationship between multiple directorships and accretive share buyback to MBEF.

3.6. Managerial Ownership

Johari et al. (2008) identified positive relationship between managerial ownership and earnings management. The authors found that the more managerial owns the shares the greater they manage earnings. Cheng, Warfield and Ye (2011) said that managers with stock ownership involve in earnings management to increase firms share prices. To avoid earnings disappointments that drops the share prices, these managers intention are higher to meet or beat EPS forecast. In year after earnings announcement, managers sell their shares that benefit from increased in value accordingly. There is no doubt that managers' private benefits increases at the expense of shareholders. The findings of Cheng et al. (2011) and Johari et al. (2008) contradict to agency theory. However the authors' finding is not in agreement with agency theory. Jensen and Meckling (1976) said that the conflict between shareholder and manager can be reduced through forming bonding activities between the two parties. This bonding activity creates managerial (director) ownership structure, which reduces manager's personal private benefits. Saleh et al. (2005) and Alves (2012) found negative relationship between earnings management and managerial ownership. Alves (2012) identified that managerial ownership decreases the level of earnings management which ultimately improves the firms' earnings quality. This develops the final hypothesis;

H6: There is a negative relationship between managerial ownership and accretive share buyback to MBEF.

The following paragraph discussed on the controls variables used for this study. *Cash levels:* Firms needs more cash for real activities manipulation relative to accruals manipulation. Therefore, firms with more cash use buybacks to manage earnings to meet or beat earnings forecast (Hribar et al., 2006). *Firm size:* Bhushan (1989) said that analyst focused more on larger firms relative to smaller firms. This gives larger firms more pressure to engage in earnings management to MBEF. Shen and Chih (2007) reported that larger firms are under closer scrutiny such as investments banks and analyst. This leads the large firms to manage earnings. *Number of Analyst:* Yu (2008) reported that more analyst coverage lesser the firm's earnings management activities. This is because the managers are aware that they are at a higher risk of getting caught involving in earnings management activities. *Big 4 Auditor* (AUD 4): The earnings management activities are lesser in firms with high quality auditor (Gul, Lyn & Tsui, 2001). Johari et al. (2008) used Big-4 Auditors as the control variable for their study. The authors believe that firms with Big-4 auditor will have less earnings management activity.

4. DATA AND METHODOLOGY

A total of 220 Malaysian listed firms engaged in accretive share buyback that meets or beats EPS forecast from year 2001 to 2008. As the sample observation is collected from year 2001, the scope of this study covers MCCG 2000. The information on accretive share buyback, board independence, CEO duality, board size, board meetings, multiple directorship and managerial ownership are obtain from the Annual Reports available in the Bursa Malaysia website. The EPS forecast information from year 2001 to 2008 is collected from Thomson DataStream through Institutional Brokers' Estimate System (IBES). The beginning and basic EPS forecast is used similar to Hribar et al. (2006). The actual annual EPS data for year 2001 - 2008, is obtained from the annual reports on Bursa Malaysia websites as per the firm's financial year.

This study use Hribar's model to measure the accretive share buyback as the earnings management model.

Pre-buyback EPS (PEPS) is computed as:

$$PEPS = NE / (OShares + [Av * IS])$$

Where:

PEPS	=	Pre-buyback EPS
NE	=	Reported annual earnings
OShares	=	Outstanding shares at the beginning of the year
Av	=	Average (0.5) number of share issued during the year
IS	=	Share issued during the year

The pre-buyback (as-if) EPS is computed to measure what would be the EPS without share buyback. The pre-share buyback EPS (PEPS) is calculated by dividing the reported annual earnings by the outstanding shares at the beginning of the year plus share issued during the year.

To estimate accretive share buyback:

$$AEPS = REPS - PEPS$$

Where:
AEPS = Accretive Share Buyback
REPS = Reported (Post-buyback) EPS
PEPS = Pre-buyback EPS

To identify whether the share buyback is an accretive share buyback (AEPS) or an earnings management device to manage earnings (MBEF), the actual EPS after share buyback (REPS) is expected to be more than a minimum of 1 cent against the pre-share buyback EPS (PEPS).

The OLS regression model is used for this study. The accretive share buyback firms that MBEF are the dependent variable (BUYVOLUME) for this study. The independent variables are the six corporate governance variables and followed by the four control variables stated in the model below. This study used accretive share buyback volume for MBEF firms as the dependent variable simply because under Bursa Listing Requirements (Chapter 12) a firm is required to submit a proposal of the buyback intention to Bursa Malaysia and then send circular to shareholders for the purpose of buyback implementation before conducting an extraordinary general meeting (EGM) or annual general meeting (AGM) to get the shareholders' approval before buybacks are allowed. Therefore, the board of directors (corporate governance mechanism) proposed the intention of buyback in terms of volume of shares to the shareholders and the actual value in Ringgit Malaysia will not be known until the actual buyback activity takes place in the open-market buyback program. Thus, accretive share buyback volume is used as the dependent variable and corporate governance mechanisms used as the independent variables to determine the relationship between corporate governance mechanism (board of directors) and accretive share buyback to MBEF.

The linear model used to test the relationship as follows:

$$BUYVOLUME_i = \alpha + \beta_1 BDINDPDC_i + \beta_2 CD_i + \beta_3 BDSIZE_i + \beta_4 BDMEET_i + \beta_5 MULTIDIR_i + \beta_6 MANOWNER_i + \beta_7 CL_i + \beta_8 TA_i + \beta_9 NOANALYST_i + \beta_{10} BIGAUDFIRM_i + \varepsilon_i \quad (1)$$

Where:

i	:	Firm
BUYVOLUME	:	Accretive share buyback volume that MBEF (unit of shares) for the year (log).
Board Independent (BDINDPDC)	:	Number of independent non-executive directors divided by total number of board of directors.

CEODUALITY (CD) : Equal 1 if CEO and Chairman is the same person (no separate position) and 0 otherwise.
Board Size (BDSIZE) : Total number of directors on the board.
Board Meeting (BDMEET) : Total number of board meetings conducted in a year.

Multiple Directorships (MULTIDIR) : Proportion of Directors on the board of the company having at least one additional directorship in another company to total number of directors on the board.

Managerial Ownership (MANOWNER) : Percentage of Directors in managerial capacity (CEO / Executive Chairman/ Executive Directors) owns direct ownership
Cash Levels (CL) : The ratio of firm's beginning of the year cash and cash equivalents to total assets.
Firm Size (TA) : Size is the logarithm of total assets at the beginning of the year
Number of Analyst (NOANALYST) : Number of Analyst forecasted on the first day of the fiscal year EPS forecast.
Audit Firm (BIGAUDFIRM) : Value of 1 if the firm engage Big-4 audit firm and value of 0 otherwise

5. RESULTS

Table 1 presents the variables that are used to observe the relationship between accretive share buyback volumes with corporate governance mechanism.

Table 1: Descriptive Statistics for 220 Accretive Share Buyback (MBEF)

							Percentiles	
	Mean	**Median**	**Std Dev**	**Skew**	**Min**	**Max**	**Lowest**	**Highest**
Accretive Share Buyback-BUYVOLUME (Volume Mil.)	7.152	1.765	17.346	5.388	0.001	151.825	0.716	5.807
BDINDPDC	0.403	0.375	0.092	1.161	0.300	0.670	0.333	0.444
CD	0.136	0.000	0.344	2.134	0.00	1.000	0.000	0.000
BDSIZE	8.196	8.000	2.118	0.936	5.000	15.000	7.000	9.000
BDMEET	5.168	5.000	1.269	1.222	4.000	10.000	4.000	6.000
MULTIDIR	0.627	0.667	0.270	-0.468	0	1.000	0.400	0.857
MANOWNER (%)	9.978	2.201	15.651	1.830	0.000	61.64	0.2537	12.339
Control Variables								
CL	0.111	0.089	0.108	1.894	-0.130	0.790	0.336	0.1702
TA	20.151	19.979	1.270	0.799	17.470	24.090	19.173	20.727
NOANALYST	5.668	3.000	6.381	1.823	1.000	26.000	2.000	6.000
BIGAUD FIRM	0.691	1.000	0.463	-0.832	0	1.000	0	1.000

From the 220 samples in Table 1, the average accretive share buyback volume is 7.152 million. The maximum volume accretive share buyback is 151.825 million with the value of RM1,079,914,000. The minimum accretive share buyback is 1,000 units of shares for the value of RM7, 000. The variance between accretive share buyback volumes between mean of 7.152 and median of 1.765 are large. Therefore, the accretive share buyback volume has been transformed into logarithm volume. By using the logarithm volume of accretive share buyback produce a mean of 14.891 and median of 15.

The first corporate governance variables used for this study is board independence (BDINDPDC). Board independence is defined as the number of independent non-executives directors divided by total number of board of directors. From Table 1, average board independence is 0.403 (40.3 percent), followed by the lowest percentile of sample is less than 0.333 (33 percent). This reveals that majority of samples are within the requirement of the Code of Corporate Governance which require one third (1/3) or 33 percent proportion of independence non-executive directors from the total number of directors (Johari et al., 2008). However, the average of 40.3 percent of board independence evidence that there is still domination of insiders by 60 percent in the samples board composition. The CEO duality (CD) is equal to 1 if the CEO and Chairman are the same person and 0 otherwise. It is observed that from the 220 samples nearly 13.6 percent is in a CEO duality position. This means that majority of the samples CEO and the Chairman are not holding the same position. This result above is similar to Johari et al. (2008) that only 10.3 percent out of the 224 samples with CEO duality position. The average board size (BDSIZE) is 8. For board meetings (BDMEET) the mean is 5 (5.168) with maximum 10 board meetings in a year. The multiple directorships (MULTIDIR) result shows on average 0.627 (62.7) directors having directorships in other firms. The descriptive statistics result for managerial ownership (MANOWNER) presents that on average 10 percent (9.978) of the directors having direct ownerships.

The following Table 2 shows the Pearson correlation results of accretive share buyback (earnings management proxy) with the corporate governance mechanisms and control variables.

Table 2: Correlations of Accretive Share Buyback and Variables

	ACCSB	BDINDPDC	CD	BDSIZE	BDMEET	MULTIDIR	MANOWNER	CL	TA	NOANALYST	BIGAUDFIRM
N	220	220	220	220	220	220	220	220	220	220	220
ACCSB	1	-.042	.197**	.26**	.174**	-.48**	-.264**	.203**	.122*	.350**	.073
BDINDPDC	-	1	-.050	-.400**	.091	.074	.123*	-.179**	-.131*	-.238**	-.016
CD	.-	-	1	.057	.106	-.18**	.078	.016	-.011	.216**	-.221**
BDSIZE	-	-	-	1	-.015	-.126*	-.191**	.174**	.128*	.313**	-.045
BDMEET	-	-	-	-	1	-.123*	-.171**	.034	.003	.185**	-.171**
MULTIDR	-	-	-	-	-	1	.142*	-.131*	-.017	-.121*	.032
MANOWNER	-	-	-	-	-	.-	1	-.099	-.013	-.121*	.112*
CL	-	-	-	-	-	-	-	1	.145*	.221**	.015
TA	-	-	-	-	-	-	-	-	1	.186**	-.012
NOANALYST	-	-	-	-	-	-	-	-	-	1	-.126*
BIGAUDFIRM	-	-	-	-	-	-	-	-	-	-	1

Notes: ** Correlation is significant at the 0.01 level; * Correlation is significant at the 0.05 level.

Table 3 presents the results of the multiple regression of accretive share buyback (earnings management proxy) with the corporate governance mechanisms and control variables.

Table 3: Regression Results of the Accretive Share Buyback and Variables

	Coefficients	**t-value**	**VIF**
Dependent variable			
Accretive Share Buyback- ACCSB (BUYVOLUME)			
Independent Variables			
Board Independence (BDINDPDC)	0.139	2.374*	1.220
CEODUALITY (CD)	0.127	2.220*	1.156
Board Size (BDSIZE)	0.142	2.366*	1.272
Board Meeting (BDMEET)	0.058	1.036	1.124
Multiple Directorship (MULTIDIR)	-0.380	-6.848**	1.090
Managerial Ownership (MANOWNER)	-0.185	-3.282**	1.126
Control Variables			
Cash Levels (CL)	0.069	1.231	1.102
Firm Size (TA)	0.065	1.181	1.061
Number of Analyst (NOANALYST)	0.228	3.778**	1.292
Big-4 Audit Firm (BIGAUDFIRM)	0.181	3.250**	1.097
Number of Observations: 220			
F-statistic: 14.571**			
R-squared: 0.411			
Adjusted R-squared: 0.383			

Notes: ** Significant at 0.01 level; * Significant at 0.05 level.

The R-squared is 0.411 and F statistics results of 14.571 at 1% significant level. This study predicted that greater the board independence (BDINDPDC) lesser the earnings management through accretive share buyback. This is also consistent with agency theory, more outsiders' increases monitoring mechanism that reduces the agency cost. However, the outcome of the results reported positive coefficient of 0.139 with a t value of 2.374 (5% significance level), this means that board independence increased by 1% and other variables such as CEO duality, board size, board meeting, multiple directorships, managerial ownerships and control variables are held constant, accretive share buyback volume increased by 0.139 unit of shares. This interprets that firms with more board independence greater will be the involvement in accretive share buyback to MBEF. Therefore, this indicates that accretive share buyback (ACCSB) and board independence are positively related. However, this study result is different from Johari et al. (2008) study that documented negative relationship between earnings management and board independence.

This study found positive coefficient for accretive share buyback and CEO duality (CD) at 0.127 (5% significance level). The results are however consistent with Saleh et al. (2005) study reported positive coefficient of 0.153 which means that CEO duality and earnings management are significantly related. Further in line with Nahandi et al. (2011) study, reported positive coefficient of 0.041 at the 5% significant level for CEO duality and earnings management. The positive coefficient of accretive share buyback (ACCSB) with board size (BDSIZE) is at 0.142 (5% significance level). Hence, this indicates that large board size encourages firms to MBEF through accretive share buyback. Furthermore, the outcome is consistent with Rahman and Ali (2006) reported a positive coefficient of 0.113 that interprets a positive significant relationship exist between board size and earnings management. This regression results further strengthen on the positive relationship of CEO duality with accretive share buyback and board size with accretive share buyback.

The result reported non-significant relationship between accretive share buyback (earnings management proxy) and board meetings (BDMEET) with coefficient at 0.058. The results showed positive coefficient but not significant between accretive share buyback and board meetings. The finding is unable to justify the nature of relationship between board meetings and accretive share buyback in the context of real activity manipulation as the earnings management proxy. However, the outcome of this study is contrary to Gulzar and Wang (2011) finding, the authors found that more board meetings held in a firm is able to reduce earnings management activities.

This study also finds a significant negative relationship between accretive share buyback and multiple directorships (MULTIDIR) and accretive share buyback and managerial ownership (MANOWNER). For accretive share buyback and multiple directorships reported negative coefficient of -0.380 with the t value of -6.848 (1% significance level). The results reveal that the increase of directorship in another firm reflects the tendency of the concern firm involvement in accretive share buyback to MBEF is gradually reduced. Followed by accretive share buyback and managerial ownership showed also negative coefficient of -0.185 (1% significance level). Similarly this interprets that with other variables held constant, accretive share buyback volume decreases by 0.185 units of shares if managerial ownership shares increases by 1 percent. The outcome of this study proves that the presence of multiple directorships and managerial ownership is able to reduce earnings management (Saleh et al., 2005) through accretive share buyback. This is also in line with Alves (2012) study that managerial ownership and earnings management is negatively related.

Among the four control variables used for this study only number of analyst (NOANALYST) and Big-4 audit firm (BIGAUDFIRM) showed significant relationship with accretive share buyback. Both control variables shown the existence of positive relationship of number of analyst and accretive share buyback with positive coefficient of 0.228 (1% significance level); Big-4 audit firm with accretive share buyback with positive coefficient of 0.181 (1% significance level). However the number of analyst with accretive share buyback result is not coinciding with Yu (2008) study, reported negative association of number of analyst and earnings management. As for Big-4 audit firms, the results are inconsistent with Johari et al. (2008) study found insignificant relationship between earnings management and Big-4 audit firm. The reason for positive relationship between Big-4 audit firms and accretive share buyback as the real activities manipulation is not easily detectable by auditors. For cash levels (CL) and firm size (TA) the results are insignificant with accretive share buyback when tested with corporate governance variables.

5.1. Additional Analysis on Large Managerial Ownership and Accretive Share Buyback

Johari et al. (2008) study found that earnings management and managerial ownership are positively related at the significant value of 1 percent. Consistently, the authors also found that large managerial ownership (above 25 percent) encourage more the earnings management activities. This shows that through Johari's study there is consistency in their findings, the managerial ownership and larger managerial ownership encourage earnings management activities. Therefore, the negative coefficient between accretive share buyback and managerial ownership result in Table 3 shows that managerial ownership discourages the accretive share buyback activities. This study expects the large managerial ownership above 25 percent (similar to Johari et al., 2008) also to discourage accretive share buyback activities. Thus, further analysis is conducted to investigate the nature of relationship between large managerial ownership and accretive share buyback. For this regression analysis, a dummy variable for large managerial ownership (value of 1 for managerial ownership above 25 percent and value of zero for managerial ownership below 25 percent) is used in the model [2]. The variables in the linear model [2] are the same as the variables in the linear model [1] except for the exclusion of managerial ownership (MANOWNER and replaced with large managerial ownership (LARGEMANOWN) variable as follows:

$$BUYVOLUME_i = \alpha + \beta_1 BDINDPDC_i + \beta_2 CD_i + \beta_3 BDSIZE_i + \beta_4 BDMEET_i + \beta_5 MULTIDIR_i + \beta_6 MANOWNER_i + \beta_7 CL_i + \beta_8 TA_i + \beta_9 NOANALYST_i + \beta_{10}\, BIGAUDFIRM_i + \varepsilon_i \quad (2)$$

The regression results mainly to show the relationship outcome between accretive share buyback and large managerial ownership are presented in Table 4. The R-squared reported for this model is 0.392. The negative coefficient results of 0.115 (t value of -2.035) for accretive share buyback and large managerial ownership is significant at 5% level. Apparently, the relationship between accretive share buyback with other variables (corporate governance and control variables) coefficient directions and significant levels are similar to the original regression results for this study in Table 3. This result proves that not only managerial ownership discourages accretive share buyback (refer to Table 3), large managerial ownership also plays an important role in discouraging the accretive share buyback activities (refer to Table 4). The finding on the negative relationship between accretive share buyback and large managerial ownership supports Lee and Hwang (2012) study on 323 sample firms from year 2005 to 2008 to observe the effect of managerial ownership and earnings management. The authors discovered that the alignment effects of agency theory works effectively in reducing earnings management activities with large managerial ownership.

6. DISCUSSION AND CONCLUSION

The result for the board independence and the accretive share buyback is contradicting to agency theory. The agency theory documents that more outsiders (board independence) are able to solve the agency issues between principals and managers. This reflects that earnings management activities can be controlled and monitored with the existence of board

Table 4: Regression Results of the Accretive Share Buyback and Variables (Further Analysis on Large Managerial Ownership)

	Coefficients	t-value
Dependent variable		
Accretive Share Buyback- ACCSB (BUYVOLUME)		
Independent Variables		
Board Independence (BDINDPDC)	0.133	2.237*
CEODUALITY (CD)	0.113	1.954*
Board Size (BDSIZE)	0.154	2.533*
Board Meeting (BDMEET)	0.072	1.263
Multiple Directorship (MULTIDIR)	-0.387	-6.880**
Large Managerial Ownership (LARGEMANOWN)	-0.115	-2.035*
Control Variables		
Cash Levels (CL)	0.076	1.352
Firm Size (TA)	0.066	1.188
Number of Analyst (NOANALYST)	0.226	3.676**
Big-4 Audit Firm (BIGAUDFIRM)	0.170	3.015**
Number of Observations: 220		
F-statistic: 13.501**		
R-squared: 0.392		
Adjusted R-squared: 0.363		

Notes: ** Significant at 0.01 level; * Significant at 0.05 level.

independence. Interestingly, the result claims that board independence are positively related to accretive share buyback to MBEF. This is in contrast to Johari et al. (2008) findings that the independent board members are competent in detecting earnings managements. However, Johari et al. (2008) used accrual manipulations as the earnings management proxy in their study. Thus, the board independence has the competence to detect and discourage earnings management through accruals manipulation activities which is easily detectable by the auditors and creates accounting scandals in the firms (Graham et al., 2005). As for real activities manipulation such as accretive share buyback will not create any accounting scandals and is not easily detectable by outside directors or auditors because it is within the ordinary course of business activities. Moreover, share buyback is an activity allowed to Malaysian listed firms by Companies Act 1965. Apparently, Rahman and Ali (2006) pointed out that the capability of the board independence in carrying out their monitoring roles is ineffective due to existence of management dominance over the board matters. Based on the descriptive statistics in Table 1 is found that the mean for board independence or the outside directors is 40.3. This reflects that more than 50 percent of the board members are still management. Therefore, it proofs on the existence of the management dominance in making the board decisions which is consistent with Rahman and Ali (2006) argument. Even there is management dominance; the board independence required to be at their best roles in monitoring skill to be in line with agency theory. Rahman and Ali (2006) further quoted that if the board failed to function well, it would be detrimental to a firm and investors. This is reason why Corporate Governance Blueprint 2011 urged board independence to act independently and at best interest of the firms.

According to this study, CEO duality is positively associated with accretive share buyback to meet or beat EPS forecast. Thus, the hypothesis is supported. This is consistent with Saleh et al. (2005) and Nahandi et al. (2011) studies that CEO duality reduces board effectiveness in discouraging earnings management. According to Nahandi et al. (2011), agency theory posits that combined leadership position do not increase firm performance so firms require to split the roles of CEO and Chairman as recommended in Cadbury Report 1992. Saleh et al. (2005) also strongly recommends to Bursa Malaysia to separate the CEO and Chairman roles for effective monitoring mechanisms. In Corporate Governance Blueprint 2011 reported that existence of conflict of interest when CEO is also the Chairman of the firm. This will raise a question of balance of power issue between CEO and board independence. Because, it affects the board independence capability on their exercise of judgments once they are beholden by the management. Thus, Corporate Governance Blueprint 2011 highlights on the separation of the roles between CEO and Chairman so that both parties can focus on their respective responsibilities. In order for the board independence to work effectively is important to split the roles between CEO and Chairman. However, this MCCG 2012 is effective from 2012 annual reports that firms can opt for separating CEO and Chairman roles on a voluntary basis for effective board independence functionality.

As for board size, this study acknowledges that large board size positively related with accretive share buyback to meet or beat EPS forecast (MBEF), similar to previous study of Rahman and Ali (2006). Thus, the hypothesis is supported. Rahman and Ali (2006) reported that large board size weakens the board monitoring mechanism on managers' actions. Nahandi et al. (2011) also noted that large board size heightens the manager's opportunistic behavior which increases on the firm's earnings management activities. In accordance with Corporate Governance Blueprint 2011, board size should be optimal to a firm with combination of effective skills and participation. In sum, board size should be a contributor not a root cause. As such, the large board size can be one of the root causes to encourage accretive share buyback to MBEF. Thus, firms should have an optimal board size with well combination of group dynamics and expertise to keep earnings management activities under control.

Based on the outcome of this study, no significant relationship is identified for board meetings and accretive share buyback. Conversely, Gulzar and Wang (2011) found that more meetings improvise board monitoring which helps in decreasing earnings management. For this study, it is identified that most firms from the sample observations on average had 5 annual board meetings only. Therefore, this study is unable to conclude whether board meeting encourages or discourages the accretive share buyback to MBEF. In sum, the encouragement or discouragement of accretive share buyback activities cannot merely determine from the number of board meetings. Thus, in order to make the board meetings as an effective monitoring mechanism to reduce earnings management, the directors' commitment in terms of time and attention in the meeting are important. The subject matter discussion in the board meetings must be based on thoughtful contribution and effective deliberation process by the board members. As stated in the Corporate Governance Blueprint 2011, the directors urge to spent sufficient time in reviewing well the materials discussed in the board meetings. This is the reason why this study failed to identify the nature of relationship between board meeting and accretive share buyback. In sum, earnings managements could not be discourage or detected through number of board meetings, it can only be detected through strong deliberations of board members in the meetings.

Multiple directorships posit a better monitoring skill in controlling firm's agency problem (Fama & Jensen, 1983). This is because they attain skills, knowledge and expertise to efficiently monitor on the managers activities (Hashim & Rahman, 2011). Thus, multiple directors are diligent monitors (Hashim & Rahman, 2011). This study found that the multiple directorships relationship is significantly negative to accretive share buyback to MBEF. Consistently, the hypothesis is supported. The outcome of this study is similar to Saleh et al. (2005) study that multiple directorships are an important monitoring mechanism. Thus, firms with multiple directorships discourage accretive share buyback to MBEF.

As in Saleh et al. (2005) and Alves (2012) studies, this study identified that the managerial ownership has a significant negative relationship with accretive share buyback to MBEF. The bonding relationship between the principals and the agents as addressed in the agency theory decreases conflict of interest between the both parties which ultimately strengthen the monitoring mechanism. Further, the study of Kamardin and Haron (2011) identified that managerial ownership is a significant monitoring mechanism in aligning managers' decision making with investors' interest. According to Mustapa and Che Ahmad (2011) managerial ownership and firm monitoring cost are negatively related as predicted by the agency theory. The authors found that when managers hold shares in the firm, lesser the information asymmetry and create an incentive to monitor the firm. Similarly, the finding of this study proves that when the managers become part of the shareholders, lesser the managers' opportunistic behavior to encourage the firms to involve in the accretive share buyback to MBEF. Thus, this indicates that managerial ownerships discourage earnings management through accretive share buyback. The finding of this study also reveals that large managerial ownership gives positive impact to discourage firms to involve in accretive share buyback to MBEF. Morck, Shleifer and Vishny (1988) study on the relationship between managerial ownership and firm value, highlighted that large managerial ownership (beyond 25%) increases the firm value where the entrenchment level of the managers are minimal. Morck et al. (1988) supports the finding of this study that large managerial ownership discourages accretive share buyback to MBEF. Apparently, the finding of this study shows that managerial ownership and large managerial ownership discourage the accretive share buyback activities.

Overall this study proves that the corporate governance mechanisms have an impact on earnings management through accretive share buyback. This study concludes that board independence must have sufficient knowledge on real activities manipulation and free from management dominance, to separate CEO and Chairman position, to maintain an optimal board size, quality board meetings with strong deliberations and thorough discussion from directors, more directorships in other firms and increased in managerial ownership will discourage the accretive share buyback to MBEF. The responsibility to implement firms best practices through strong corporate governance to mitigate earnings management activities not only rest with the board of directors as the central agent between shareholders and management. It should be a joint effort of internal and external stakeholders to reduce firms' involvement in earnings management activities to achieve the short-term strategies and set more emphasis in achieving the long-term strategies to increase the firm value. Therefore, the external stakeholders for example shareholders or investors should not penalize the firms for failing to MBEF (a short-term strategy) rather support the firms in achieving their long-term objectives. This study sample observations starts from year 2001 to 2008. Thus, for corporate governance measures this study used MCCG 2000. However, this study recommends the future study to use corporate governance measures as in MCCG 2012 to investigate nature of relationship between corporate governance mechanism and accretive share buyback to meet or beat EPS forecast.

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