# Related Parties Transactions, Family Firms and Fraudulent Financial Reporting in Malaysian Public Listed Companies

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**Abstract:** This research examines the factors which influence fraudulent financial reporting in 158 Malaysian public listed companies from the year 2017 until 2021. The current study applies the quantitative approach and focuses on the issue whether related party transactions and family firms influence the fraudulent financial reporting. Fraudulent financial reporting is debated globally due to the increased number of occurrence year by year. Stakeholders are directly impacted by the fraudulent financial reporting cases over the year with million and billion losses reported. Public listed firms need to be transparent in publishing annual report, therefore it is pertinent to conduct early assessment in investigating factors which influence fraudulent financial reporting. Family firms and related party transactions are among the factors that were argued in past literatures. The significant findings indicate family firms influence fraudulent financial reporting therefore contribute to the determinants of fraudulent financial reporting in Malaysian public listed firms and suggests some prevention of strategy.

**Keywords:** Fraudulent financial reporting, earnings management, family firms, related party transactions.

## 1. INTRODUCTION

Financial fraud is a financial crime involving manipulation of financial reports that often results in harsh punishments and fines for those involved. In the Malaysia landscape, among the scandals that arise are Port Klang Free Zone scandal, Transmile Group Berhad and recently 1Malaysia Development Berhad scandal (Hashim, Salleh, Shuhaimi, & Ismail, 2020). According to PwC's Global Economic Crime and Fraud Survey – Malaysia Report (2020), the fraud cases in Malaysia remains high which brings out the amendment of section 17A of the Malaysian Anti-Corruption Commission (MACC) Act 2009 that comes into effect on 1st June 2020 establishing corporate liability for corruption offences. Moreover, according to the Association of Certified Fraud Examiners (ACFE) 2020 report, the percentage of Southern Asia occupational fraud scheme of financial statement is 12%, which is in the fourth rank of overall 11 types of occupational fraud. According to the report, financial statement fraud contributed to the biggest losses in term of monetary value to the firm.

Since the 1970s, Malaysia had published financial reports in accordance with International Accounting Standards (IAS) (Ball, Robin, & Wu, 2003). Among the agencies that oversight the corporate reporting for public entities in Malaysia are Securities Commission of Malaysia (SC), Bursa Malaysia Stock Exchange, Malaysian Institute of Accountants (MIA) and Companies Commission of Malaysia (CCM). Malaysia as the developing country also had established capital market and securities laws, company regulations and statutory audit and disclosure requirements (Lau & Ooi, 2016) which governed by various government agencies. Although there are already enforcement of law and agencies in Malaysia, the corporate scandals in Malaysia public firms still alarming as per data presented by the KPMG Malaysia Fraud, Bribery and Corruption Survey in 2013 discovered that fraud cases increased by nearly 100% over the past three years in Malaysia (KPMG, 2013). The issues raise attention on the need to implement more stringent market regulations, and specialists, as for example, the Securities Commission of Malaysia (SC) together with Bank Negara Malaysia (BNM) need to have greater requirement of enactment in order to wipe out the issues (Norwani, Mohamad, & Tamby Chek, 2011).

Abdullah, Mohamad Yusof, and Mohamad Nor (2010) studied the incident of financial restatements from 2002 until 2005 in Malaysian public listed firms and discovered that revenue and cost misstatements accounted for 54 percent of financial fraud cases. The research is in line with ACFE yearly report which emphasized the occupational fraud that is also known as fraudulent financial reporting occurred frequently. The Star Online (2016) stated that, since three years earlier, the incidence of financial statements fraud has risen with an increasing rate of 14 per cent. The increasing rate impose negative impact in Malaysia itself that affecting all the stakeholders. Securities Commission Malaysia (2019) shows that there were 34 ongoing criminal and civil cases at various levels of courts whereby 26% related to corporate

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governance breaches such as financial misstatement and false disclosure.

## 2. LITERATURE REVIEW

Fraudulent financial reporting (FFR) which is also known as earnings management is where financial report is altered and not presented in the fairly manner to mislead the users of the financial report in order for personal or business gains. Malaysia rating in terms of earnings management considered as worst due to Malaysia ranks in the top 10 positions among 34 countries (Bhattacharya, Daouk, & Welker, 2003). The preparers of the financial report are accountable to produce the true and fair view of figures so that the stakeholders can make informed business decisions. Generally, managers tend to manipulate the financial reports since they possess additional advantages through internal information of the firm. In 2009, KPMG Malaysia conducted a survey report which showed the estimated value of fraudulent financial reporting amounted to 63.5 million per year. According to the 2020, PwC's Global Economic Crime and Fraud Survey financial statement fraud remained top five from 14 incidents of fraud which is equal to 28%.

Malaysian market in term of family owned business is more than half of total market which is around 56% (Stijn Claessens, Fan, & Lang, 2006). This means, more than half of the Malaysian market is influenced by ownership control of family affiliated. According to Kim and Yi (2006) self-dealing transactions can be facilitated by complex company group structures, which prevents outside investors from being able to keep an eye on the transactions and implies that one of the key elements that increases the likelihood of earnings management is business group affiliation. According to Fama and Jensen (1983) the presence of the founding family as the shareholder with a substantial stock stake or largest shareholder and the ability to oversee management gives the family an edge in monitoring the business. This view shown that there is possibility of red flag occur in the circulation of earnings management. Furthermore, the ownership of family firms means that there is internal planning and discussion between the family members in the event of controlling the firms. The interest of maintaining the image of the family also can be a plot twist in decision-making process for the well-being firms.

According to Malaysian Financial Reporting Standard (MFRS) 124 which is equivalent to International Accounting Standard (IAS) 24: Related Party Disclosures, related party transactions (RPTs) are the transfer of resources, services, or obligations between a reporting entity and a related party, regardless of whether a price is charged. It is compulsory for all firms that are registered as separate legal entity, whether private limited or public limited, to disclose the related party transactions in the audited report. Prior research argued between whether RPTs brings harm or unharmed to the firms itself (Fooladi & Farhadi, 2017; Kohlbeck & Mayhew, 2010; Sharkar, Sobhan, & Sultan, 2007; Li et al., 2022; Smith & Marx, 2022). The extent of Malaysian firms to create holding and subsidiary company had shown various firms structure. For example, a public listed firm in Malaysia usually have many subsidiaries in order to diversify the income stream. Furthermore, the RPTs create alarming alert in term of shadow economy, where firms tend to evade the tax by setting up a dummy firm with no actual business operations (Pacini & Wadlinger, 2018). In most of these frauds, managers used RPTs to generate misleading financial statements and enrich themselves (Fooladi & Farhadi, 2019).

This study uses the stakeholders' theory as the underpinning theory. According to Mercier (1999) stakeholders are "all the representative that are concerned about the firm's growth and good condition". Freeman (1984) defines stakeholders' theory as "the awareness of firm's objectives which can affect or be affected by any individual or group". Furthermore, Caroll (1989) differentiated between primary and secondary stakeholders which refers to agents who are impacted directly through contractual relationship and impacted without contractual relationship respectively. Firms that applied the stakeholder approach are likely to evolve the firms into specific management implementation practice which fulfil their stakeholders and organizational target (Russo & Fouts, 1997). Managers who fail to sustain the relationship with the stakeholders may face the consequences in term of financial (Tse, 2011).

### 2.1. Research Framework

Fig. (**1**) below shows a research framework of this study. This exploration employs factors which may influence the fraudulent financial reporting, being family firms and related party transactions. The added control variable is the firm's size to avoid any potential bias.

### 2.2. Hypotheses Development

Over the years, earnings management has been widely discussed globally and Malaysia also had been affected. Most Malaysian companies are directly interested, as is usual of Asian businesses. Most of them are family-controlled. Yueng (2002) reports that Malaysia is ranked second in Asian region just behind Indonesia in aspect of the percentage family-owned listed firms in the Asian. Conflicts among family members may result in fewer disclosures and an increase in earnings management because of different business objectives, unfair treatment by related family members, or, to some extent, unhealthy competition among family members themselves (Gómez-Mejía, Haynes, Núñez-Nickel, Jacobson, & Moyano-Fuentes, 2007; Setia-Atmaja, Haman, & Tanewski, 2011; Belesis al., 2022; Nurhadi al., 2022). The alignment effect theory suggests that in order to sustain the reputation and interest between the family members and shareholders the activities of earnings management will decreased (Wan Mohammad & Wasiuzzaman, 2020). According to Shamsul Nahar Abdullah and Mohd Nasir (2004) the share is owned by the top twenty stockholders, the majority of whom are family members. Since family members own major shareholding which give them powers to make decision (Teh, Ong, & Ying, 2017) this gives rise to probability of fraudulent financial reporting to occur in the events when business in financial distress, meanwhile, in the same time, firms need to protect the firms image and business. Findings by Fan and Wong (2002) indicated that the intention to falsify financial reporting was found to be positively associated with business ownership. According to Rahman, Biswas, and Kirkham (2006) firms are owned by family founders and

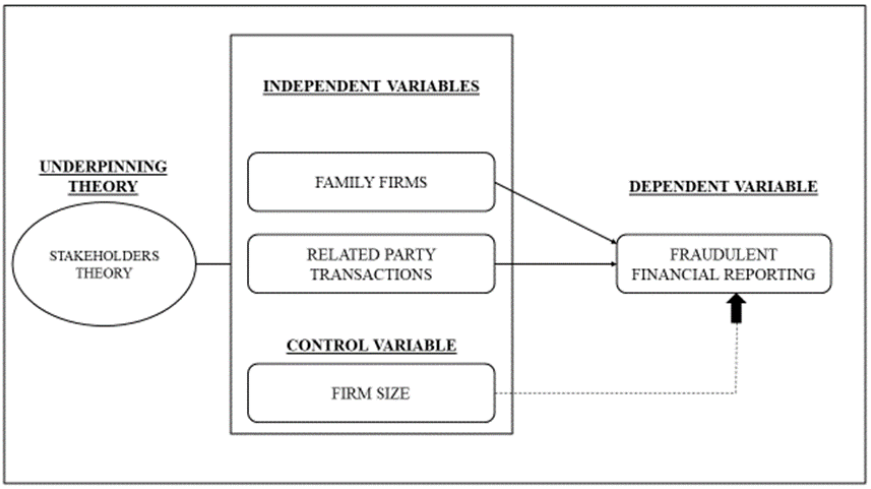


**Fig. (1).** Research framework.

their heir which suggest that many public listed firms are family inherited and restrained. According to Ngui (2002) around half of Malaysia's Gross Domestic Product (GDP) is generated by family businesses. Le and Buck (2011) reported that as ownership concentration rises, company financial performance improves, but the impact of foreign and institutional ownership is negligible. Kim and Yi (2006) reveal that in Korea, enterprises linked with Chaebols business groups have a higher prevalence of earnings management than firms that are not affiliated. The development in prior research on the effect of earnings management through family firms therefore in this study we developed the following hypotheses as per below:

H1: Family firms influence significantly fraudulent financial reporting

Related party transactions (RPTs) is one of the main disclosure in the annual report of public listed firms. Khanna and Palepu (2000) imply that in the context of emerging countries, interactions among enterprises in a group can help individual firms in the group run more effectively than standalone firms. This view supported Malaysia as the developing country status. As for example, the firms in the group having financial difficulties in obtaining external funds can obtain the financial support from other firms in the same group. Consistent with this example, Gopalan, Nanda, and Seru (2007) reported that financial aid amongst enterprises in the same group is vital, according to the research, and is utilised to relieve the load of the weaker firms (Shin & Park, 1999). Managers or controlling owners make their accounting information less proportional to their industrial partners in order to avoid detection by government authorities through illegal usage of RPTs (Lee, Kang, Lee, & Park, 2016) can option to use offensive accounting practice through RPTs (Sherman & Young, 2001). RPTs may violate the arm's-length assumption of regular transactions, impairing the representational faithfulness and verifiability of accounting data (Wang & Yuan, 2012). Prior studies have investigated that RPTs such as sales and services, purchases or inter-company loans impacted earnings management (Aharony, Wang, & Yuan, 2010; Saleh, Jaffar, & Yatim, 2013; Ahmad al., 2022; Esan al., 2022; Mubeen al., 2022). Malaysian Accounting Standard Board (MASB) revised Financial Reporting Standard 124, "Related party disclosures," in 2008. The primary goal of MASB in revising FRS 124 is to monitor the RPTs process and mitigate the opportunistic behavior of related parties. Another explanation for RPTs is that they are not adverse to shareholders and that they are an efficient transaction that rationally satisfies economic demands that bind the party to the company (Hasnan, Daie, & Hussain, 2016). Gordon and Henry (2005) debated that RPTs could be more potent than entering a similar transaction with an outside party as argued by Hasnan, Abdul Rahman, and Mahenthrian (2008) where it may be beneficial for the firms to engage with firms in the group due to they are contractual related to the group therefore less motivation for the firms to manipulate earnings. Based on the previous study, thus the following hypotheses is developed:

H2: Related party transactions significantly influence fraudulent financial reporting

## 3. RESEARCH METHODOLOGY

### 3.1. Population and Sample

The population of the study is the Malaysian Public Listed Companies listed on the Main Market. As of 26th April 2022, 982 companies were listed in the Main Market Bursa Malaysia. The total sector in the Main Market of Bursa Malaysia comprising of 15 sectors namely closed-end funds, construction, consumer products and services, energy, financial services, health care, industrial products and services, plantation, property, real estate investment trusts, special purpose acquisition company, technology, telecommunications and media, transportation and logistics, and utilities.

This study chose a total of 158 companies in Malaysian Public Listed Company over the 5 years consecutive period ranging from 2015 until 2021. Roscoe (1975) suggested that for most studies, a sample size greater than 50 and less than 500 are suitable. Hence, this is consistent with the sample of this study. Green (1991) proposed an equation to determine sampling size for regression analysis as $N \geq 50+8m$ (where m refers to the number of independent variable in the model). Hence, this study consist of 2 independent variable, $N \geq 50+8(2) = N \geq 66$. Therefore, this study which comprises of

**Table 1. The Variable Measurements.**

| Variables | Proxies | Labels | Measurement | Prevailing Literature |
|---|---|---|---|---|
| Dependent Variable: Fraudulent Financial Reporting | PN17 firms | FFR | Dummy variable consist of value 0 and 1. Unhealthy firms (PN17) = 1<br>Healthy firms = 0 | Arshad et al. (2015). |
| Independent Variables: Family Firms | 1. Equity ownership of controlling family<br>2. No of controlling family in board of directors | 1. EQ<br>2. BOD | 1. Percentage of shares owned by all controlling family members<br>2. No of controlling family members in BOD / total no of BOD. Measured in percentage. | La Porta et al. (1999); Claessens et al. (2000), Tai (2017). |
| Independent Variables: Related Party Transactions (RPTs) | 1. RPTs amount over sales<br>2. RPTs amount over total assets | 1. RPTS<br>2. RPTA | 1. Percentage of RPTs amount over total sales : RPTs / total revenue x 100%<br>2. Percentage of RPTs amount over total assets : RPTs / total assets x 100% | Elizabeth A. Gordon et al. (2004), Cheung et al. (2006). |
| Control Variable: Firm Size | Total assets | FSIZE | Natural *logarithm* of total assets at the end of fiscal year period : *log* (total assets) | Watts and Zimmerman (1990) |

158 samples firm is consistent with the suggestion by Roscoe (1975) and Green (1991).

### 3.2. Data Collection Method

The study applies the secondary data approach. Information is collected from respective companies' annual report that is readily and available in Bursa Malaysia Berhad website. Data selection was taken from the period of 2015 until 2021 which coincides the period where the global pandemic of Covid-19 occur globally that also affected companies in Malaysia. The sample of 158 listed companies were carefully selected according to PN17 status of companies which retrieved from Bursa Malaysia website (https://www.bursamalaysia.com/bm/trade/trading_resources/listing_directory/pn17_and_gn13_companies) in each consecutive years from 2015 – 2021. The PN17 status of listed companies then were match with the non-PN17 status from the main market according to business sector for each consecutive 5 years from 2015 until 2021. The non-PN17 companies were selected randomly with control in firms' size to avoid any potential bias. PN17 firms with no annual report were excluded from the data collection together.

### 3.3. Variables Measurement

#### *3.3.1. Dependent Variable*

***Fraudulent Financial Reporting***

This study aims at whether family firms and related party transactions influence fraudulent financial reporting in Malaysian Public Listed firms. According to Arshad, Iqbal, and Omar (2015) the tendency to manipulate earnings among public listed firms are more likely to happen in financially distress company in order to improve their financial. According to Bursa Malaysia Securities Berhad, firms that are in financial distress categorized as PN17 obliged to propose regularization plan accordingly. In this study, PN17 firms are taken as proxy of fraudulent financial reporting which consistent with study by Arshad et al. (2015) and compared with firms that are not listed as PN17. The comparison is match with the same year and business sector from 2017 until 2021. This variable is measured through dummy variable which is, if the firms are PN17 considered as unhealthy firms the value is set to 1 and healthy firms the value is set to 0.

#### *3.3.2. Independent Variables*

The variable that may influence fraudulent financial reporting in this study are family firms and related party transactions. The two independent variables are further discussed below:

***Family Firms***

The variable is measured through the equity ownership in the firm. Consistent with previous studies by La Porta, Lopez-de-Silanes, and Shleifer (1999) and Claessens, Dyankov, and Lang (2000), family firms are defined when an entity or person owns minimum of 10% from the total equity or served as largest shareholders. Furthermore, the surname of equity ownership is also included in determining the family firms. Since Bursa Malaysia required public firms to disclose any family relationship, data are analyzed in the annual report through the sections Board of Directors profile. Then analysis of shareholding was analyzed further to determine the total equity owned by the all the controlling family members. The second criteria to measure family firms is through whether any of the controlling family sits in the board of directors consistent with study by Tai (2017). Thus, both criteria are measured through percentage of equity ownership and percentage of controlling family sits in the board of directors. If any of both criteria is met, then the firms are defined as family firms (Tai, 2017). This information is also readily extracted from annual report since it is a disclosure requirement by Bursa Malaysia to all public firms' annual report.

***Related Party Transactions***

Bursa Malaysia requires all the listed firms to comply with disclosure of related party transactions in annual report. Related party transactions define by Bursa Malaysia as a transaction entered into by the listed issuer or its subsidiaries which involves the interest, direct or indirect, of a related

party. Related party transactions are available at notes to the accounts in the annual report. RPTs are first measured through the amount of RPTs disclosed in the annual report and divided by the total revenue of group. RPTs are then further measured through the RPTs amount over total assets. These two measurement are crucial since high RPTs amount over 10% from total revenue or total assets are considered high RPT and potentially triggered conflict of interest(Gordon, Henry, & Palia, 2004) and expropriation of stakeholders' interest (Cheung, Rau, & Stouraitis, 2006).

***Firm Size***

This study uses natural logarithm of total assets as measurement of control variable. Watts and Zimmerman (1990) found that big companies tend to practice earnings management which consistent with this study to test whether family owned firms and RPTs influence earnings management. Since firm size could influence the outcome of this study, hence, it is appropriate to choose firms' size as the control variable.

Table **1** summarizes the dependent, independent and control variables.

### 3.4. Regression Model

Below is the multiple regression model constructed for this study

$FFR = \beta_0 + \beta_1 (EQ) + \beta_2 (BOD) + \beta_3 (RPTS) + \beta_4 (RPTA) + \beta_5 (FSIZE) + \varepsilon$

Where:

EQ = percentage of shares owned by controlling family

BOD = percentage of controlling family as director in total number board of directors

RPTS = the amount of RPTs over total revenue

RPTA = the amount of RPTs over total assets

FSIZE = natural log of total assets

$\varepsilon$ = random error

## 4. DATA ANALYSES

### 4.1. Descriptive Analysis

Table **2** shows the demographic profiles of the study sample. Out of 158 sample firms of public listed companies in Malaysia, majority were from Industrial Product & Services (27.8%) followed by Energy (24.1%), Consumer Products & Services (19.0%), Property (11.4%), Technology (2.5%) while Telecommunications & Media, Financial Services and Transportation & Logistics each recorded 5.1%.

**Table 2. Demographic Profile.**

| Item | Frequency | Percentage (%) |
|---|---|---|
| Sector | | |
| Consumer Products & Services | 30 | 19.0 |
| Industrial Products & Services | 44 | 27.8 |
| Energy | 38 | 24.1 |
| Telecommunications & Media | 8 | 5.1 |
| Property | 18 | 11.4 |
| Financial Services | 8 | 5.1 |
| Transportation & Logistics | 8 | 5.1 |
| Technology | 4 | 2.5 |

### 4.2. Normality Test

Table **3** illustrates the normality analysis scores for each of the six variables from 158 public listed companies in Malaysia to check the normality of the data.. From Table 3, the measure of skewness for all variables fall between -0.336 and 0.846. The general statistical measure of skewness ranging from -1.0 and 1.0 is considered normally distributed and acceptable enough to conduct any of the parametric analysis (Teh et al., 2017). Since the measures of skewness for all variables are within the range between -1.0 and 1.0, it can be concluded that the distribution of the scores do not depart from normality. Hence, the required assumption for using the parametric statistical procedures for further analysis is satisfied.

### 4.3. Correlation Analysis

Correlation generally describes the effect that two or more phenomena occur together and therefore they are linked. This can be range from -1 to 1. This study used the Pearson Correlation test to examine whether EQ, BOD, RPTS, RPTA and FFR does have relationship.

**Table 3. Descriptive Statistics for All Variables.**

| Variables | No. of sample | Min. score | Max. score | Std. Deviation | Skewness | Kurtosis |
|---|---|---|---|---|---|---|
| FFR | 158 | 0 | 1 | 0.5015 | 0.000 | -0.026 |
| EQ | 158 | 0 | 56.77 | 13.6938 | 0.846 | 0.542 |
| BOD | 158 | 0 | 55.56 | 16.2555 | 0.782 | -0.473 |
| RPTS | 158 | 0 | 610.97 | 16.8463 | 0.127 | 0.944 |
| RPTA | 158 | 0 | 1340.78 | 12.6929 | 0.732 | 0.179 |
| FSIZE | 158 | 4.32 | 11.88 | 1.1703 | -0.336 | 0.062 |

**Table 4. Summary of Correlation Analysis.**

| Variables | FFR | EQ | BOD | RPTS | RPTA | FSIZE |
|---|---|---|---|---|---|---|
| FFR | 1.000 | | | | | |
| EQ | -0.024* | 1.000 | | | | |
| BOD | -0.060* | 0.376* | 1.000 | | | |
| RPTS | 0.183* | 0.006* | 0.009* | 1.000 | | |
| RPTA | 0.112* | -0.042* | -0.015* | 0.028* | 1.00 | |
| FSIZE | -0.566* | -0.141* | -0.036* | -0.157* | -0.305* | 1.00 |
| *N = 158, All value in * are significant (p < 0.05)* | | | | | | |

Table **4** indicates that the p-value between EQ and FFR less than α= 0.05. With the value of r=-0.024, it showed that EQ and FFR have negative relationship with little relationship. Therefore, it can be concluded that there has negatively weak significant relationship (r=-0.024) between EQ and FFR. With the value of *r*=-0.060, it showed that BOD and FFR have negative relationship with little relationship. Therefore, it can be concluded that there has negatively weak relationship *(r=-0.060)* between BOD and FFR.

The value of p-value between RPTS and FFR on Table **4** shows that it was less than α= 0.05. Since the r = 0.183, it means that RPTS and FFR have positive relationship with little relationship. In conclusion, there is a significant positive moderate relationship (r=0.183) between RPTS and FFR. Other than that, at the p-value between RPTA and FFR is less than α= 0.05. Therefore, there is a relationship between RPTA and FFR. With the value of r=0.112, it showed that RPTA and FFR have positive relationship with little relationship.

### 4.4. Multiple Regression Analysis

Multiple linear regressions were conducted to check the effect between dependent variable and independent variables. All measurement of independent variables (EQ, BOD, RPTS and RPTA) were regressed on the dependent variable (FFR). The results of this study are to answer the objective which is to determine the factors that influence fraudulent financial reporting in Malaysian public listed companies.

#### *4.4.1. Overall F-Test for Significance of Regression*

The ANOVA test was used to test the significance of the regression model. The result from Table **5** shows that the regression model is significant since the p-value of 0.000 less than α=0.05.

**Table 5. Overall F-Test for Significance of Regression.**

| Source of Variation | Sum of Squares | Degree of Freedom | Mean Square | F-value | Significant P-value |
|---|---|---|---|---|---|
| Regression | 13.729 | 5 | 2.746 | 16.195 | 0.000 |
| Residual | 25.771 | 152 | 0.170 | | |
| Total | 39.500 | 157 | | | |

#### *4.4.2. Individual T-Test for Significance of Individual Predictor Variables*

Based on the Table **6**, it showed that four measurement of independent variables which are EQ, BOD, RPTS and RPTA were regressed to predicting FFR. This study used level of significant at α=0.05. The results showed that only two variables which is EQ and BOD are significant towards FFR while RPTS and RPTA does not have significant effect towards FFR in Malaysian public listed companies.

**Table 6. Individual T-Test for Significance of Individual Predictor Variables.**

| Terms | Unstandardized Coefficients | | t-value | Significant p-value |
|---|---|---|---|---|
| | B | Standard Error | | |
| (Constant) | 2.722 | 0.272 | 9.989 | 0.000 |
| EQ | -0.034 | 0.026 | -7.292 | 0.020 |
| BOD | -0.015 | 0.022 | -6.681 | 0.045 |
| RPTS | 0.001 | 0.001 | 1.417 | 0.158 |
| RPTA | 0.000 | 0.000 | -1.085 | 0.280 |
| FSIZE | -0.253 | 0.030 | -8.348 | 0.000 |

Note: Dependent Variable (Y) is FFR.

Table **6** indicates that EQ has significant influence on the FFR with *p-value* = 0.020 which is less than α = 0.05. This means that EQ is strong enough to influence the fraudulent financial reporting in Malaysian public listed companies. Other than that, BOD which was also the measurement for family firms, also have influence towards FFR. BOD has significant influence on the FFR with p-value = 0.045 which is less than α = 0.05.

Table **6** depicts that RPTS does not influence the FFR. This is due to at α = 0.05, the p-value of RPTS is 0.158 which is more than α = 0.05. This result showed that RPTS does not give any influence on fraudulent financial reporting in Malaysian public listed companies. Also from Table 6, at α = 0.05, the result showed that RPTA have p-value = 0.280 which is more than α = 0.05. It means that RPTA does not have significant influence on the FFR. These results indicated that fraudulent financial reporting in Malaysian public listed companies does not influence by RPTA. The result from the measurement of RPTs find that RPTs did not influence FFR contradict with previous studies by Gordon and Henry (2005); Hasnan et al. (2016) which found that RPTs influence earnings management. This study result shown that it is consistent by the stricter rules enforcement by Bursa Malaysia on RPTs through their Chapter 10 Listing Requirement that detailed out all the RPTs compliance.

#### *4.4.3. Goodness of Fit*

Table **7** depicts the value of R-square is 0.348. This means that the model explains 34.8% of the variation in the FFR. 65.2% is explained by other factors. Adjusted R-square is 0.326. These indicate that the model explains 32.6% of the

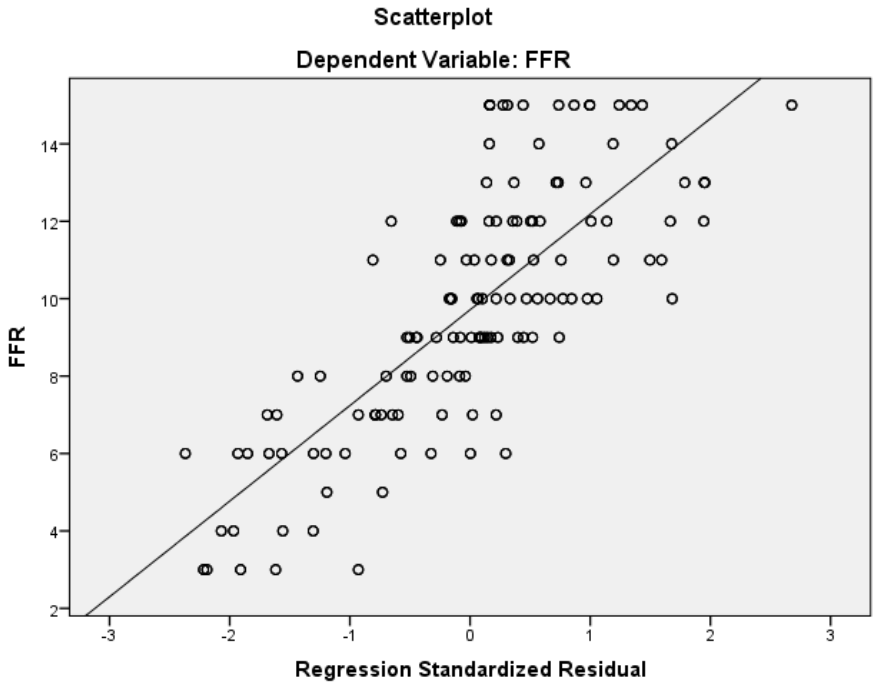


**Fig. (2).** *Scatter Plot of FFR vs. Independent Variables.*

variation in the FFR after considering the sample size and the number of independent variables while 67.4% is explained by other factors.

**Table 7. Model Summary.**

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|---|---|---|---|---|
| 1 | 0.590 | 0.348 | 0.326 | 0.4118 |

### *4.4.4. Multicollinearity Assumption*

Multicollinearity will occur when two or more independent variables in a regression model provide redundant information about the response and highly correlated to each other. The estimation of β and interpretation can be serious a problem in the presence of the multicollinearity. Table **8** presents that the value of VIF for each measurement of independent variables (EQ = 1.196, BOD = 1.165, RPTS = 1.026 and RPTA = 1.112) are less than 10 and the value of the Tolerance for each of the independent variables measurement (EQ = 0.836, BOD = 0.858, RPTS = 0.975 and RPTA = 0.899) are more than 0.1. The result shows that the presence of multicollinearity does not exist and the multicollinearity assumption are satisfied.

**Table 8. VIF and Tolerance Values.**

| Variables | Collinearity Statistics | |
|---|---|---|
| | VIF | Tolerance |
| EQ | 1.196 | 0.836 |
| BOD | 1.165 | 0.858 |
| RPTS | 1.026 | 0.975 |
| RPTA | 1.112 | 0.899 |
| FSIZE | 1.160 | 0.862 |

### *4.4.5. Linearity Assumption*

Linearity checking is one of the multiple linear regression assumptions that need to be satisfied. The relationship between the dependent variable and the independent variables need to be linear. This assumption can be checked by plotting the scatter plot on FFR against residual. Graphs on Figure 2 shows a positive linear relationship between FFR and residual because the scores are close and moving upwards to the right. Thus, the assumption of linearity is not violated.

## 5. DISCUSSION OF FINDINGS

Family firms as the independent variable were measured through two proxies. This study found that the first measurement which is equity ownership of the controlling family in the firms does have low significant negative relationship with fraudulent financial reporting.

The second measurement of family firms which is the number of controlling family in board of directors does have low significant negative relationship with fraudulent financial reporting. Therefore, H1 is accepted. As per previous study by Teh et al. (2017) Malaysian public listed firms are usually owned by family members as the largest shareholders of the firms. The ownership of firms by controlling family members will trigger conflict of interest such as to retain the image of family members as the owners of the firm which will attract the probability of doing immoral behavior in ensuring financial reporting which looks inspiring in the eyes of other stakeholders. The single concentrated firms will incur the

conflict between the principal and agent as per discussed in the agency theory. This is because, when firms are owned by family, the decision of any matter arise will be jeopardized since there is a probability that the decision are made not in line with other stakeholders since family firms as the largest shareholders have the veto power in making decision. Even though Bursa Malaysia does regulate the requirement to disclose any family relationship in the annual report, it still does not refrain any individual or entity to own shares. Hence, based on the findings of this study, it is crucial for the enforcement agency and regulator of this country to regulate and improvise the Companies Act to ensure that Malaysian public listed firms are not owned by family. This is one of the ways to ensure all stakeholders interest is being taken care of and equally distributed without any conflict-of-interest issue. Firms' size as the control variable indicates that when firms' size is being controlled, family firms influence fraudulent financial reporting.

Related party transactions as the independent variable were measured through the amount of RPTs over total revenue and the amount of RPTs over total assets. The amount was taken up based on group amount since public listed firms are consolidated based on group. Based on findings from sample of data, related party transactions do not influence fraudulent financial reporting. Therefore, H2 is not accepted.

Related party transactions were disclosed in the annual report through the notes in the accounts which is a requirement by Bursa Malaysia. Even though RPTs did have relationship with FFR, it did not influence fraudulent financial reporting. The relationship of RPTs and FFRs were found consistent with previous literature by Hasnan et al. (2016) which found that RPTs are negatively associated with earnings quality. Since RPTs disclosure are made as the mandatory requirement in public listed firms' annual report, it gives a positive impact to the public listed firms in Malaysia in ensuring that stakeholders interest is preserved.

The structure of public listed firms in Malaysia which comprises of holding and multiple subsidiary company does inflict the opportunity in financial reporting manipulation which will affect stakeholders' interest, whereby if there is no strict requirement and enforcement by authority, the chances of earnings management manipulation are high. The collaboration by the International Auditing Standard (IAS) together with Malaysia Accounting Standard Board (MASB) in determining the scope of related party transactions and the enforcement by the Malaysian authority namely Bursa Malaysia effectively hindering from RPTs are being manipulated. Therefore, from the result, it can be concluded that even RPTs did not influence FFR due to well established rules and regulation by the authority which in turn made the firms in Malaysia are very well discipline enough to comply with the strict requirement by Bursa Malaysia. Firms' size as the control variables in this study indicates that when firms' size is being controlled, RPTs did not influence FFR.

### 5.1. Limitations and Recommendations for Future Research

This current study investigates on the factors which influence fraudulent financial reporting in Malaysia public listed firms. This study selected five years period which inclusive of global pandemic period from 2017 until 2021 which could reflect the true potential of FFR occurred. The business sectors were chosen based on the PN17 firms. The limitation of this current study is firstly on the measurement of independent variables. This study only employs two independent variables, whereby, to further assess FFR, future research can add up variable of politically exposed persons (PEP). Since PEP are one of crucial issues being discussed worldwide and Malaysia also exposed to the risk of involvement PEP in public listed firms, therefore, it is recommended for future research to conduct further test on the additional variable.

## 6. CONCLUSION

Fraudulent financial reporting is the global issues which triggers the needs to further assess on what and why it happens, so that precautionary measures can be taken. It is said that prevention is better than cure. If you can prevent it from happening, then the damage is not crucial.

Public listed firms are firms that are involved with various stakeholders such as shareholders, suppliers, customers, government, society and others. Due to involvement of many parties, there is a need of stricter rules and regulations from the enforcement authority. The growth of a country depends on the well-mannered and observed business transactions. This means, financial reports need to be presented in the true and fair view so that all the investment decision by the stakeholders can be carried out in positive manner. The size of the firms in the public listed firms are relatively big, which means the preparer of the financial report must be competence enough and the assessment of financial report must be assessed by independent party so that no conflict of interest arises.

In conclusion, this study finds that family firms influence FFR while RPTs did not influence FFR. Concentrated ownership by family members needs to be evaluated so that fraud incidence can be avoided. If Bursa Malaysia can impose strict requirement of RPTs to prevent any manipulation of business transactions, then, there should be ways for the authority in ensuring firms in Malaysian are not dominated by family because family firms are proven influencing FFR in this study.

With the aim to attract potential foreign investors, the findings from this study demands the authority or policy maker to further improvise the rules and regulation of public listed firms. It is imperative to the administrator of the company, to check for abnormalities or irregularities of financial statements before submission to Bursa Malaysia to keep from any potential backfire that could harm its reputation. This study concludes that pre assessment prevention tools in detecting fraudulent financial reporting is crucial to avoid fraud occurrence.

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