ANTECEDENTS AND ISSUES INFLUENCING
FINANCIAL DISCLOSURE: A CASE STUDY OF
MALAYSIAN LOCAL GOVERNMENT

Submitted by
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A thesis submitted in total fulfillment
of the requirements for the degree of
Doctor of Philosophy

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ABSTRACT

The primary purpose of this study was to understand and explain the financial disclosure practices and disclosure management in Malaysian Local Authorities (MLAs). Applying Gibbins, Richardson and Waterhouse (1990) model, the study sought to illuminate how decisions regarding disclosure are made, and how institutional factors, environmental factors, and external auditors influenced such decisions in MLAs. In order to achieve the aims of this research, a case study approach was adopted. The case study was conducted in 5 MLAs consisting of one city council, three municipal councils and one district council.

The field research evidence suggests that the financial disclosures are authorized at the higher level within the council. Disclosure position is influenced by significant organizational and environmental antecedent conditions. These include organizational influences such as a collective management view, previous practices, council culture, number of professionals and desire of the council to become more transparent. Environmental influences include legislation, standards and regulations, and the disclosure practices of other councils. Further, the results indicate that the accountants working in MLAs routinely seek and generally follow advice from external auditors, whom they regard as the source of reference especially pertaining to disclosure issues.

This study contributes to the existing literature by providing a greater understanding of the disclosure management and practice in the public sector, particularly at the Malaysian local government level. By applying Gibbins et al. (1990) model that embraces both organizational and environmental influences on disclosure strategy to the public sector, it overcomes the weaknesses of previous disclosure studies in taking into account the organizational and environmental factors. It also makes a contribution in terms of methodology in that case studies research provides important insights into the complex and multi-dimensional phenomenon of disclosure. From the practical stance, this study offers guidance to practitioners by providing evidence that they could learn a lot from other councils’ experiences which could indirectly improve the disclosure practices in their councils. Further, this study offers guidance to the regulators and legislators by outlining significant organizational and environmental influences on disclosure decision as they may wish to take cognisance of these factors in developing external rules and regulations concerning financial disclosure in MLAs.
Acknowledgements

First and foremost, I praise and thank God the Almighty for blessing me with the opportunity to pursue my degree of Doctor of Philosophy and for giving me the strength and patience to complete this research. Many people deserve recognition and appreciation for the completion of this thesis.

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Statement of Authorship

Except where reference is made in the text of the thesis, this thesis contains no material published elsewhere or extracted in whole or in part from a thesis submitted for the award of any other degree or diploma. No other person’s work has been used without due acknowledgement in the main text of the thesis. This thesis has not been submitted for the award of any degree or diploma in any other tertiary institution.

All research procedures reported in the thesis were approved by the relevant Ethics Committee.

_____________________
Neilson Anak Teruki

October 2012
Dedication

This thesis is dedicated to my mother, my siblings and my friends for their love and support..........
CHAPTER ONE
OVERVIEW OF THE STUDY

1.0 Introduction and Background of the Study

There are many studies on financial disclosure and they have investigated a wide range of issues both in the private and public sector as well as both in developed and developing countries. Many of these researchers (e.g. Haniffa & Cooke, 2002; Eng & Mak, 2003; Prencipe, 2004; Cahan, Rahman & Perera, 2005; Chavent, Ding, Fu, & Stolowy 2006; Mohd-Ghazali & Weetman, 2006; Alsaeed, 2006; Iatridis, 2008; Wang et al., 2008; Hossain & Hammami, 2009) have taken an interest in a firm characteristics that could predict its disclosure level. However, the majority of these studies have employed conventional statistical methods to test empirical hypotheses and have been subjected to several criticisms. For example, Watt and Zimmerman (1986) argued that “the use of statistical methods has often produced inconclusive and counter-intuitive results” (p. 718). There are several reasons for such criticism including the application of imprecise proxies, different sample sizes, inadequate sampling methods, and mis-specified functional models (Watt & Zimmerman, 1986).

Compared to the private sector, studies investigating disclosure practices in the public sector are limited. Some studies on the public sector (e.g. Evans & Patton, 1987; Ingram & DeJong, 1987; Giroux, 1989; Christiaens, 1999; Gore, 2004) looked at the incentives for financial disclosure. Various incentives have been identified for the accounting choice with some studies providing mixed and conflicting results. Furthermore, due to various measures of accounting disclosure used in some studies, the research findings are difficult to compare.

However, there is a dearth of empirical studies about who in the organization makes particular disclosure decisions, the range of issues considered when making disclosure decisions, the role of external mediator (s) in disclosure practices as well as reasons for disclosing financial information in local government contexts. This thesis is conducted by means of field-based research. This is deemed to be appropriate considering the dearth of disclosure studies employing field-based research in the literature. This thesis adds to the literature by addressing the above issues and by examining financial
disclosure in public sector organisations, particularly financial disclosure practices in Malaysian local government.

The focus on public sector financial disclosure arises from the fact that in recent decades the public sector has been subjected to criticism such as inefficiency, lack of flexibility and accountability, poor performance, imperious bureaucracy and corruption (Siddiquee, 2006; Tooley, Hooks & Basnan, 2010a). With regards to Malaysian local authorities, public interest in the performance of local authorities in Malaysia has risen in terms of the delivery of services. Tooley, Hooks and Basnan (2010b) state that some ratepayers and the state governments are beginning to express dissatisfaction over the performance of local authorities and are seeking greater accountability from local authorities. The public and other stakeholders have started to question the transparency and integrity of local public servants in delivering services (The Sun, August 30, 2005; The Sun, January 20, 2006; The Sun, February 17, 2006).

It has been argued that the public and other stakeholders cannot make an informed judgement on the performance of local authorities unless information is provided (Tooley et al., 2010b). Financial reports have been identified as one of the main mechanism available for local authorities to communicate information about their activities (Ryan, Stanley & Nelson, 2002; Kloot & Martin, 2001; Hyndman & Anderson, 1995). Financial information is perceived as one of the tools for decision-making helping understand how the entity’s inflows, outflows, assets, liabilities, surpluses and deficits affect their own interests and expectations (Borgonovi & Anessi-Pessina, 2000). It is in this context that local government accounting is increasingly expected to provide stakeholders with a “true and fair” view of the entity’s performance. Therefore, the emphasis is placed on the role of accounting systems in measuring and evaluating both financial and service performance, promoting disclosure and communicating results to stakeholders (Steccolini, 2004). Internationally, financial information in local government is normally disclosed by two types of reports, these being internal financial reports to managers and councillors and external financial reports to external stakeholders such as taxpayers, the relevant Minister and government authority (Pilcher & Dean, 2009).

The disclosure of public sector financial information is a traditional way of meeting the stakeholders’ needs to inform them about the public sector activities and their
contribution to the social and economic development (Perez, Bolivar & Lopez Hernandez, 2007). One widely accepted objective of financial disclosure is to allow stakeholders to access information so they can gauge whether the objectives of the organisation are being discharged and to assess its performance (Mack & Ryan, 2007). Similarly, financial information is an important aspect whereby its disclosure allows an entity to demonstrate its internal and external achievements (Lee, 2008; Tooley et al., 2010b). Many researchers have discussed the importance and usefulness of financial reporting to users of the public service (see for example, Alijarde, 1997; Jones & Puglisi, 1997; Tayib, Coombs & Ameen, 1999; Mignot & Dolley, 2000; Mack & Ryan, 2006). It is suggested that financial information provided by public service organizations should help users assess the ability of such organizations to manage their affairs and resources efficiently and effectively (GASB, 1987).

It is generally recognised that a key document in disclosing financial information to external users - primarily the legislature, government oversight bodies, creditors and citizenry - is the government’s financial reports (Ryan, Stanley & Nelson, 2002; Hyndman & Anderson 1995).

While most countries issue local government financial information, it has often been pointed out that citizens have difficulty in accessing it (Tayib et al., 1999), which in practice implies a lack of information transparency, availability and understanding of complexity. Although the role of financial reports in rendering local government accountable is often emphasised, the existence and identity of financial report users is often debated and the actual use of the financial report is not clearly known (Steccolini, 2004). Previous studies have failed to reach a consensus as to the identity of the users of financial statements and their information needs (Steccolini, 2004) and is still the subject of ongoing debate in the public sector. Furthermore, there is evidence that local government financial reports are not extensively used by the public particularly because: they were unaware of their existence (Tayib et al., 1999), the number of users is likely to be small (Jones, 1992), the financial statements are complex (Stanley, Jennings & Mack, 2008) and that a report may not be directly available (see Tayib et al., 1999).

In Malaysia, local government represents the third tier of government and “grass roots” government or the “government closest to the people” (Phang, 2008b). Working at the forefront of dealing with local communities means having direct working relationships
with external stakeholders. Local government is a public agency that provides urban services and is accountable to the citizens as well as the state and federal governments that financial assistance or grants (Kuppusamy, 2008). Tooley et al. (2010b) state that the public has a number of provisions allowing them to gain access to information regarding the performance of local authorities and to provide feedback. These provisions include: section 23 of Act 171 that requires the meetings of local authorities be open to the public and representatives of local media; section 27 of the Act allowing the tax payer to inspect the minutes of the proceedings of the local authority; and section 60 (4) of Act 171 requiring audited financial accounts to be published in the government gazette. In addition, section 142 of Act 171 provides that “citizens who are dissatisfied with the authorities’ performance have a right to make objections in writing and are allowed an opportunity of being heard at the consequent enquiry”. Ratepayers and consumers can claim a right to information so they can make informed judgements about plans and actions undertaken by their local government. The Malaysian Local Authorities (MLAs) are also answerable to a hierarchy of regulators, policy-makers, and other oversight bodies at the state and federal levels of government (Othman, Taylor, Sulaiman & Jusoff, 2008). As a consequence, inefficiencies and poor performance of MLAs may come to reflect poorly on the state governments and affect their political popularity since they are directly answerable to their respective state government (Tooley et al., 2010b).

Although many researchers acknowledged the importance and usefulness of financial reporting to public service users (see Jones & Puglisi, 1997; Tayib et al., 1999; Mignot & Dolley, 2000), the role of the financial report in rendering government accountability and to meet the users’ needs is often questioned in MLAs. This may be due to the greater difficulty in accessing the MLAs’ financial information. As revealed by Tayib in Tayib et al. (1999), easy access to annual financial accounts is limited to councillors, auditors, the State Authority and the Ministry of Housing and Local Government (MHLG). Tayib et al. (1999) also found that no local taxpayers in their sample had access to financial information because they were unaware of its existence. Furthermore, not all MLAs prepare an annual report since it is not mandatory and only by those having adequate financial resources (Abdul Wahid, Abdul Aziz, cited in Hassan, Hassan & Nor, 2007). Another possible reason is the absence of specific financial reporting requirements (especially financial reporting standards) imposed on MLAs in preparing their annual financial accounts (Tayib et al., 1999). Any individual
who is interested in inspecting the financial accounts of specific MLAs has to wait until
the financial accounts are published in the official government gazettes, which
inevitably takes time. One possible reason for this is that the Local Government Act
1976 did not specifically prescribe the period of submission of the MLAs financial
statements for auditing (Auditor General's Report, 2007).

With respect to the financial reporting in MLAs, there are no specific financial reporting
requirements, either statutory or non-statutory, currently imposed on Malaysian Local
Authorities in preparing their annual financial accounts (Coombs & Tayib, 1999;
Tooley et al., 2010b)\(^1\). Although sections 53 and 54 of the Local Government Act 1976
require Malaysian local governments to keep proper records and books of account and
prepare annual financial reports, it does not stipulate the required form and content of
the report. Instead it leaves it to the state authority to determine their form and content.
Thus the financial disclosure practises of MLAs have been largely voluntary rather than
dictated by statutory requirements (Coombs & Tayib, 1999). The absence of accounting
standards has given local authorities considerable discretion regarding the treatment of
accounting items and their presentation and disclosure in the financial reports. This
discretion has been characterized by differences in the content and format of the annual
financial accounts between the local authorities in Malaysia (Tayib et al., 1999). Tayib
et al. (1999) recommended that proper financial reporting requirements or standards be
specific to the appropriate public sector body; in particular MLAs should meet the needs
and interests of stakeholders. Although it was recommended more than a decade ago,
the state authorities, however, have yet to announce any guidelines on this matter
(Tooley et al., 2010b).

In the absence of specific statutory guidance, numerous local authorities in Malaysia
have adopted the Federal Treasury Circular (FTC) No. 15, 1994 (superseded by FTC
No. 4, 2007) – Guidance for Preparing and Presenting Annual Reports and Financial
Statements for Federal Statutory Bodies, in preparing their financial reports and
accounts (Coombs & Tayib, 1999). Furthermore, Tayib et al. (1999) revealed that not
all the financial statements required in the FTC were prepared by the MLAs. According
to Coombs and Tayib (1999), there are two major factors that prevent the development

\(^1\) Unlike the practises in well-developed countries (for example, in UK, CIPFA has developed and
implemented The Codes of Practice on Local Authorities Accounting in United Kingdom: A statement of
Recommended Practice - guidance notes for practitioners; in Australia, AAS 27 Financial Reporting by
Local Government (1991) which specific rules and regulations to govern the published accounts of local
authorities)
of local authority financial reporting in Malaysia. These are the lack of qualified accountants employed in the MLAs and the lack of involvement of professional bodies in the development of local authority financial reporting. The private sector professional bodies such as the Malaysian Institute of Accountants (MIA) and Malaysian Association of Certified Public Accountants (MACPA) do not show a significant level of interest to further improve public sector financial reporting. In addition, the Malaysian Institute of Public Sector Accounting (MIPSA) whose members are public sector accountants is expected “to provide a lead to the federal government in the development of the public sector accounting and reporting standards” (Coombs & Tayib, 1997, p. 14). However, this association according to Coombs and Tayib (1997) is “not particularly active and its establishment has not been widely trumpeted” (p. 15).

1.1 Statement of the Problem

The lack of empirical justification for the public sector financial disclosure model underlying features includes who make disclosure decision, the identification of users, the identification of antecedents/incentives for disclosure and how these antecedents influence their disclosure decision is the continuing calls for empirical research which have to date been unanswered. As a consequence, continuous research to explain these issues is necessary. Furthermore, the majority of studies on the financial disclosure were conducted in developed countries (Wang et al., 2008; Alsaeed, 2006) where the stakeholders are arguably more sophisticated and have greater capacity to exercise their rights for information compared to those stakeholders in developing countries with a smaller group of studies have examined the linkage in developing countries. Little attention has been devoted to the study of accounting disclosure in Southeast Asia Countries, more specifically in Malaysia, a rapidly emerging economy (Coombs and Tayib, 1999).

Moreover, the role of organizational and environmental factor in explaining financial disclosure has thus far not been adequately addressed. Neither has there been an attempt to use field studies (Merchant & Van der Stede, 2006; Adam, 1997) to explain the financial disclosure practices in the organization. Gibbins, Richardson and Waterhouse (1990), Adams (1997), Hopwood (2000) and Carpenter and Feroz (2001) argue that most of the previous disclosure studies do not take into account the organizational,
social and environmental factors. There has thus been a consistent failure to relate the
effect of institutional and social aspects and the quality of mandatory disclosures in
firms’ financial statements. As Hopwood (2000, p.763) has noted, “the institutional and
social aspects of financial accounting are still relatively unexplored”. As a consequence,
there is a need to carry a study to explain the disclosure practices and management in
the public sector by incorporating organizational, social and environmental factors
(Gibbins et al., 1990; Adams, 1997). These factors are expected to have an influence on
the manager’s decision to disclose information.

There is also a need to carry out a different approach to study disclosure practices and
management, for example, by means of case study. As suggested by Craswell and
Taylor (1992, p.305), the application of field-based techniques is particularly relevant to
disclosure studies as they “may assist in providing additional explanations of
differences in disclosure policies and the extent to which proprietary costs of disclosure
vary across firms”. In a similar vein, Adams (1997, p. 731) suggested that field-based
research “could contribute insights into the complex and multi-dimensional
phenomenon of corporate disclosure and usefully complement conventional statistical
analyses”. Therefore, following Gibbins et al. (1990) and Adams (1997), this study is
conducted by means of field-based research. This is deemed to be appropriate
considering the dearth of disclosure studies employing field-based research in the
literature. To the best of author’s knowledge, there is no study been conducted to
explain the disclosure practice and management by means of field-based research in
Malaysia, particularly, in Malaysian public sector.

In Malaysia, local governments are primarily governed by three sets of acts. The main
reference of the subsidiary laws are: Local Government Act 1976 (widely known in
Malaysia as Act 171); Town and Country Planning Act 1976 (Act 172) and Street,
Drainage and Building Act 1974 (Act 133). However, Tayib et al. (1999) noted that the
Act 171 is the most important instrument for accounting and reporting purposes. It (for
example, under sections 53 and 54) requires MLAs to keep proper records and books of
account and that the annual financial report should be prepared. However, the Act does
not stipulate the required form and content of the financial reports. Instead, section 54
provides authority to the state governments to determine the form and content of such
reports. Although a study by Tayib et al. (1999) recommended that proper requirements
or standards for MLA financial reporting should be considered by the monitoring agency, the state authorities have yet to announce any guidelines (Tooley et al., 2010b). The lack of clear financial reporting requirements and standards has given the MLA considerable discretion regarding the treatment of accounting items and their presentation as well as form and content in the financial reports (Tayib et al., 1999).

As a result, the disclosure practices, particularly in terms of the form and content of financial reports in MLAs have been largely voluntarily rather than dictated by statutory requirement. The disclosure and reporting environments in MLA provide a particularly fruitful insight in which to study the antecedents and issues influencing disclosure. Malaysia’s relatively unregulated local government makes it an interesting environment to examine voluntary disclosure decisions. As argued by Adams (1997), as managerial discretion to disclose information in the financial report is not encumbered by external regulations such as statutory minimum reporting requirements and accounting standards, the influence of firm-specific factors on financial disclosure and reporting should be more evident among MLAs than among those operating in more tightly regulated jurisdictions such as that of Australia and the UK.

The remainder of this chapter outlines the research objectives and research questions and structure of the thesis.

1.2 Research Objectives and Research Questions

The regulatory structure of local government financial reporting is different from publicly owned corporations. While the latter type of corporations are all subject to the regulatory authority of the Securities and Exchange Commission, local governments face differing state government authorities and regulations (Ingram and DeJong, 1987). There has been an increase in calls for increased regulation due to corporate accounting scandals (Gore, 2004). The argument is that the “market failures necessitate mandatory disclosure, and that in the absence of regulation, organizations lack incentives to voluntarily disclose adequate levels of information” (Gore, 2004, p. 24). Ingram and DeJong (1987) argue that there should be other economic costs and benefits that dominate the decisions in unregulated local authorities since the costs of state regulations are not a factor. Rational managers will choose to disclose information that
brings more benefits than costs. This argument is supported Gore (2004) who suggests that there is an economic basis for governments’ choice to voluntarily provide financial information. Mandating more information imposes costs on governments and ultimately the taxpayers, while conferring benefits to public accountants by increasing monitoring costs. Moreover, empirical evidence found by Adams (1997) suggests that financial disclosure is influenced both by organizational and environmental factors such as company culture and tradition, industry norms and market competition. Putting these arguments together, there are many antecedents that may influence financial disclosure practices in unregulated local authorities. These factors might include organizational, institutional and market factors (see Gibbins et al., 1990; Adams, 1997). Ingram and Dejong (1987) argue that “the disclosure practices of unregulated local authorities provide a particularly useful means of examining whether incentives exist in an unregulated environment to induce disclosure” (p. 254).

The aim of this study is to understand and explain financial disclosure practices and disclosure management in MLAs. More specifically, the study seeks to investigate who makes financial disclosure decisions, the range of issues considered when making such decisions (e.g. company culture, historical precedent and tradition, internal financial regulation, dominant personalities and professional groups), the role of auditor (s) and other external parties in the disclosure process, and the influence of external disclosure rules on disclosure decisions. To the best of author’s knowledge, no empirical study to date has addressed these issues in MLAs. Therefore, the dearth of empirical studies makes it necessary to investigate them.

The research questions of this study are as follows:

1. How decisions regarding disclosure are made?
2. How does the organization disclose financial information and why does it disclose financial information?
3. What are the internal/external antecedents influence financial disclosure decisions and how do they influence financial disclosure decisions?
4. What external mediator influences financial disclosure decisions and how does it influence financial disclosure decisions?
1.3 Motivation and Significance of the Study

This study is motivated by four factors. First, it is motivated by the ongoing debate about the usefulness of financial reporting in local authorities and increasing importance and emphasis of local authority accounting particularly in Malaysian local government. Second, there have been a number of issues raised in relation to the published financial statements of local authorities in Malaysia. These include the quality of financial information reported, the preparation of accounts not following a public sector accounting standard as a result of the absence of financial reporting requirements imposed on MLAs, and evidence that local authority financial statements are not currently extensively used by the public (Hassan, Hassan & Nor, 2007; Tayib et al., 1999). Third, to the best of author’s knowledge, this study is believed to be the first field-based study to examine the disclosure practices of MLAs. Therefore, the approach followed in this study could encourage others to employ field work in future disclosure research especially in the public sector. Fourth, this research will address the organizational and environmental determinants of financial disclosure which thus far still relatively unexplored. This research thus will provide empirical data as to what organizational and environmental antecedents and issues influence financial disclosure practices in MLAs. To the best of my knowledge, there has been no research conducted in MLAs that investigate the issues and influences in the financial disclosure and reporting practices, particularly in terms of the form and content of financial reports. Therefore, an examination of voluntary disclosure provides a valuable insight into motivating factors and influences on MLAs’ financial disclosure practices.

The findings of the study are potentially useful to MLAs in a number of ways. Firstly, it is hoped that this study will provide the MLAs with a better understanding of the issues surrounding financial disclosure. This understanding would be useful in directing local managers’ efforts towards perceived deficiencies in reporting. Secondly, understanding why local government managers disclose information is potentially useful for regulators, monitoring agencies and policy-making bodies in specifying the form and content of financial reports for the purposes of accounting and reporting in MLAs. Thirdly and lastly, the study will help other local authorities whose annual reporting might be inadequate. The understanding would also be useful in directing local managers’ efforts towards perceived deficiencies in reporting as well as useful in order
to help other local government whose annual reporting is thought to be inadequate. As noted by Gibbins et al. (1992, p.3):

although there has been considerable research on the accounting information disclosed by corporations………there has been little on the process by which financial disclosure happens, on the organizational structures and deliberations involved in it, or the rather broad array of disclosure in addition to the financial statements and their associated data...

Therefore, improving our understanding on financial disclosure practices will be valuable.

1.4 Structure of the Thesis

The structure of the thesis is outlined in Figure 1-1. Chapter 2 provides an overview of Malaysian local government, including the history of its management and functions, position in the government hierarchy, and financial reporting practices. Chapter 3 reviews the literature related to financial disclosure studies in the private and public sector. This chapter is organized into four parts. The first provides an overview of financial disclosure studies. The second part reviews the managers’ disclosure decision. The third part reviews the disclosure studies in the private sector. The fourth part reviews and discusses the disclosure studies in the public sector.

Chapter 4 describes the conceptual and theoretical basis upon which this study was carried out. Chapter 5 explains the research methodology. The chapter also discusses the justifications for using the case study method and other methods. Further, this chapter describes the research design of the study, data collection procedures and methods of data analysis. The validity and reliability of evidence is also discussed.

Chapter 6 analyses how decisions regarding financial disclosure are made. The analysis is based on interviews conducted with staff of five local councils, using the following pseudonyms: Alpha, Beta, Gamma, Delta and Omega. This chapter is organized into three parts. The first part analyses the person/committee responsible for making financial disclosure decisions. The second part analyses how decisions regarding financial disclosure are made.
Chapter 7 reports the findings from interviews with the intention of answering the second research question: How does the organization disclose financial information and why does it do so? This chapter is organized into two parts. The first part analyses how MLAs disclose their financial information, and analyses how and to whom the MLAs disclose their financial information, the frequency and adequacy of disclosure and the analysis of data content and data organization in their financial statements. The second part analyses why the MLAs disclose financial information.

Chapter 8 analyses the interview evidence collected in the field and is supported by the review of documentary evidence with the intention of identifying and explaining the internal/external antecedents that influence financial disclosure decisions. The chapter also identifies the external mediator (s) and explains how it influences financial disclosure decisions. Finally, Chapter 9 presents the discussion and conclusions of the study. Furthermore, key contributions of this research in terms of theory, methodology, as well as practical recommendations are outlined. Finally, limitations and recommendations for future research are noted.
Figure 1.1: The Thesis Structure
1.5 Chapter Summary

This chapter sets out the background for the thesis by reviewing and discussing the financial disclosure studies and criticisms of financial disclosure internationally and in the Malaysian local government. The chapter also discusses the statement of the problem, research objectives and research questions, motivation and significance of the study as well as how the thesis is structured.
CHAPTER TWO
INSTITUTIONAL BACKGROUND – MALAYSIAN LOCAL GOVERNMENT

2.0 Introduction

This chapter provides an overview of Malaysian local government, its history, management and functions, position in the government hierarchy, and financial reporting practices.

2.1 Malaysian Local Government – An Overview

Malaysia is a federal constitutional monarchy consisting of 13 states and 3 federal territories with a bicameral federal legislature and unicameral state legislatures. The country achieved independence from Britain on 31st August 1957, whereupon the National Government promulgated a Federal Constitution that upholds the principles of parliamentary democracy. The federal parliament is bicameral; it consists of Yang Di Pertuan Agong (the King), the Dewan Rakyat (the Lower House or House of Representatives) and Dewan Negara (the Upper House or Senate). Members of the Lower House are elected, whereas members of the Upper House are appointed. As prescribed under Article 32 (2) of the Federal Constitution, the King has a five-year term and is appointed by the Conference of Rulers from the rulers of nine states in the Peninsula. Article 181 of the Federal Constitution sets out the executive authority of the King. The allocation of powers among the three levels of government is constitutionally determined. The federal government, which is constitutionally empowered to control the lower level of government, can be regarded as the national sovereign. Subsequently, the state government can be regarded as a quasi-sovereign while the local government is the infra-sovereign (Norris, 1980).

Administratively, Malaysia is organized along a three-tier government structure: federal, state and local (UNESCAP, 1999). In carrying out its duties as enumerated in the Federal and Concurrent Lists of the Federal Constitution, the federal government has established a number of ministries. Currently, there are 24 federal ministries, in
addition to a number of departments and agencies (The Prime Minister’s Office of Malaysia, 2009). Under the terms of the Federal Constitution, executive power is vested with the King, however, in all practicality day-to-day government is exercised by a Cabinet of Ministers led by the Prime Minister. The Cabinet is the highest coordinating executive body of all government activities and interests. The Cabinet is assisted in the discharge of its functions by two national councils, the National Economic Council (NEC), responsible for coordinating all development programs and the National Security Council (NSC), responsible for national security. To improve and enhance the machinery of government, the Federal Constitution provides further avenues of federal influence over state governments. Such influence is exercisable over matters that are even listed under the state list of the constitution. There are three other national councils, the National Council for Local Government (NCLG) under article 95A, the National Land Council (NLC) under Article 91, and the National Finance Council (NFC) under article 108.

At state level, each state has a “unicameral legislature” (UNESCAP, 1999). The state governments are headed by ceremonial state rulers. The ruler acts on the advice of the State Executive Council that is chaired by the Chief Minister. In distinct contrast to the arrangement in the federal government, all the states have unicameral legislatures (UNESCAP, 1999). The elections are held every five years. In the states where there is no hereditary ruler a governor is appointed by the King to be the ceremonial Head of State. The state legislature has the authority to pass any law so long as it is consistent with federal laws as underlined by Schedule IX of the Federal Constitution. In that sense, the state legislature is the centre of democratic policy (UNESCAP, 1999). The constitutional division of legislative power between federal and state governments is set out in the Ninth Schedule of the Federal Constitution and summarized in Table 2.1.
Table 2.1: The Constitutional Division of Powers between Federal and State Governments

<table>
<thead>
<tr>
<th>Federal List</th>
<th>State List</th>
<th>Concurrent List</th>
</tr>
</thead>
<tbody>
<tr>
<td>External affairs</td>
<td>Muslim religious law</td>
<td>Social welfare</td>
</tr>
<tr>
<td>Defence and security</td>
<td>Land Ownership and Use</td>
<td>Public health</td>
</tr>
<tr>
<td>Trade, commerce and industry</td>
<td>Agriculture and Forestry</td>
<td>Town and country Planning</td>
</tr>
<tr>
<td>Shipping, communication and transport</td>
<td>State works and water supply (when not federalized)</td>
<td>Drainage and irrigation</td>
</tr>
<tr>
<td>Water supply, rivers and canals</td>
<td>Loans for state development and public debt</td>
<td>Rehabilitation of mining land and soil erosion</td>
</tr>
<tr>
<td>Finance and taxation</td>
<td>Malay reservation and custom</td>
<td>National parks and wildlife</td>
</tr>
<tr>
<td>Education and health</td>
<td><em>Local Government</em></td>
<td></td>
</tr>
<tr>
<td>Labor and social security</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public works and utilities</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Phang (2008a, p.2)

The third level in the government hierarchy is local government or local authority (Norris, 1980). The Local Government Act 1976 categorized local government into three main categories according to population and annual revenue - the city council/city hall, municipal council, and district councils. Working on the principle of *ultra-vires* (that is, they can only undertake activities as specified in statute and in accordance with by-laws), local governments are primarily governed by three sets of acts: Local Government Act 1976 (widely known in Malaysia as Act 171); Town and Country Planning Act 1976 (Act 172); and Street, Drainage and Building Act 1974 (Act 133).

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2 The term ‘local government’ is used in the Federal Constitution. However, the terms ‘local government’ and ‘local authority’ are often used interchangeably in Malaysia (Tooley et al., 2010a). Therefore, both terms are used interchangeably in this thesis.
2.2 History of Malaysian Local Government

The present system of local government in Malaysia can be traced back to Britain, which colonized Malaysia for nearly two centuries. Norris (1980, p.4) noted that “Malaysia inherited a British legacy in terms of local government objectives and style and has been deeply influenced by British precedents”. During its formative stage most local government statutes were based on English law. However, local governments in Malaysia have evolved into “a system having its own identity, characteristics and laws that reflect the socioeconomic and political environment of the country” (UNESCAP, 1999, p.8). In Malaysia (at that time Malaya), Penang and Malacca (which were part of the Straits Settlement) were the first two states to form local governments. It was in Penang that the British formed a Committee of Assessors in 1801 and charged it with the responsibility of planning and implementing urban development. In 1828, this committee was replaced by a municipality (Kuppusamy, 2008). This development laid the foundation for the establishment of local government in Malaysia. Local councils were later set up in Malacca and other Federated and Unfederated Malay States including those in Sabah and Sarawak (UNESCAP, 1999).

To get town boards and local councils working, the British colonial government formulated various types of legislation. Regulations issued under the East India Company’s Charter\(^3\) were the first local government legislation introduced and these were followed by the Indian Legislation Act and the Municipal Rates Act in 1848 (Coombs & Tayib, 1999). Under Section 15 of the Municipal Rates Act 1848, the Municipal Committee was required to publish a statement of accounts on behalf of ratepayers (Coombs & Tayib, 1999) and subsequently provided an avenue for the public to scrutinize financial accounts, use of public funds and functions of the committee (Kuppusamy, 2008). Following this, numerous amendments and new ordinances were introduced by the British colonial government with the primary objective of improving the administration of local government.

On 1 February 1948, the federal government became the guardian of local government in Malaya and allowed for the propagation of local government across all states in the

\(^3\) At this time, it was the East India Company responsible for Penang, Malacca and Singapore (Also known as United Settlement)
peninsula. By that time, there were four municipalities (Penang, Melaka, Kuala Lumpur and Singapore), 65 town boards and four rural boards (Kuppusamy, 2008). The Local Authorities Elections Ordinance 1950 (Ordinance No. 52 of 1950) was then passed to allow for election of councillors ranging from 6 to 24 per council. On 1 December 1956, all councillors in Penang were elected while the president of the council was elected among the councillors. The Local Government Elections Act 1960 (Act 11) replaced the Local Authorities Elections Ordinance 1950 in order for it have greater legislative strength concerning local government elections (Kuppusamy, 2008). However, internal administrative and political problems facing the local councils and the violent confrontation against the newly-formed Malaysian federation by Indonesia in 1964, led to the suspension of local government elections in 1965 (UNESCAP, 1999). Since then local government elections have not been restored, though various interest groups are pushing for their revival.

After Independence in 1957, when the Federal Constitution came into existence, local government outside the federal territory was placed under the state list (UNESCAP, 1999). The problems faced by local government authorities in the 1960s were further compounded by the existence of various types of local councils as well as by the complexity of a number of different ordinances, enactments, by-laws, rules and regulations. Rules and regulations were not standardised throughout Malaya and varied according to states or territories to which they applied (Coombs & Tayib, 1999). For example, Selangor, Perak, Negeri Sembilan, Pahang, Kelantan, Terengganu, Perlis, Kedah and Johor had their own rulers and their own set of rules and regulations. Hence, the government felt a need to re-examine and reform the local government system in Malaysia. For this reason The Royal Commission of Enquiry to Investigate into the Workings of Local Authorities in West Malaysia (also known as the Athi Nahappan Report) headed by Senator Dato’ Athi Nahappan was established in 1965 to examine the working of all local authorities, review existing laws and to recommend structural changes (Kuppusamy, 2008). Even though the report was not accepted (UNESCAP, 1999) it did pave the way for the restructuring of the entire local government system through the Local Government Act 124 (Temporary Provisions) in 1973. This Act was subsequently replaced by the Local Government Act 1976 which still serves as the basis for local government today (Kuppusamy, 2008).
Following the passage of the uniform Local Government Act 124 (Temporary Provisions) in 1973, the government reviewed all basic laws regulating the powers, duties, responsibilities and functions of local authorities. Three parent laws were enacted for that purpose: Street, Drainage and Building Act 1974 (Act 133), Town and Country Planning Act 1976 (Act 172), and Local Government Act 1976 (UNESCAP, 1999).

Table 2.2: Local Governments by State

<table>
<thead>
<tr>
<th>State</th>
<th>Cities</th>
<th>Municipal Councils</th>
<th>District Councils</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Johor</td>
<td>1</td>
<td>6</td>
<td>8</td>
<td>15</td>
</tr>
<tr>
<td>Kedah</td>
<td>1</td>
<td>3</td>
<td>7</td>
<td>11</td>
</tr>
<tr>
<td>Kelantan</td>
<td>0</td>
<td>1</td>
<td>11</td>
<td>12</td>
</tr>
<tr>
<td>Melaka</td>
<td>1</td>
<td>2</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Negeri Sembilan</td>
<td>0</td>
<td>3</td>
<td>5</td>
<td>8</td>
</tr>
<tr>
<td>Pahang</td>
<td>0</td>
<td>3</td>
<td>8</td>
<td>11</td>
</tr>
<tr>
<td>Pulau Pinang</td>
<td>0</td>
<td>2</td>
<td>0</td>
<td>2</td>
</tr>
<tr>
<td>Perak</td>
<td>1</td>
<td>4</td>
<td>10</td>
<td>15</td>
</tr>
<tr>
<td>Perlis</td>
<td>0</td>
<td>1</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
<td>Selangor</td>
<td>2</td>
<td>6</td>
<td>4</td>
<td>12</td>
</tr>
<tr>
<td>Terengganu</td>
<td>1</td>
<td>2</td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>Sabah</td>
<td>1</td>
<td>2</td>
<td>19</td>
<td>22</td>
</tr>
<tr>
<td>Sarawak</td>
<td>3</td>
<td>3</td>
<td>20</td>
<td>26</td>
</tr>
<tr>
<td>Wilayah Persekutuan</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>12</td>
<td>38</td>
<td>96</td>
<td>146</td>
</tr>
</tbody>
</table>


With the completion of the restructuring exercise that took place from 1974 to 1988, the 374 local authorities (consisting of city councils, town boards, town councils, rural and district councils) were restructured into 14 municipal councils and 79 district councils in Peninsular Malaysia, 6 municipal councils and 39 district councils in Sabah and Sarawak (UNESCAP, 1999). As the economy developed, local governments were further refined and/or regrouped. Currently, there are 146 local governments comprising of 12 city halls and councils, 38 municipal councils and 96 district councils (Table 2.2).
2.3 Category of Malaysian Local Government

NCLG organized local authorities in Malaysia into three categories, namely city council, municipal council and district council. Basically, the councils are categorized based on 6 criteria: area, population, income, services, development and other facilities respectively, as shown in Table 2.3. The city council is normally the administrative centre in the state, with the population not less than 500,000 people and the annual revenue not less than RM100 million. The city council must provide a high level of services including revenue collection activities, approval of development projects, enforcement and other functions as well as have a sound organizational structure. The city council focus is on urban development which emphasizes sustainable development and addressing urban issues like squatters, illegal factories operating, safety, housing for low income groups and environmental protection. Sustainable urban indicators as emphasized in the Malaysia Urban Indicator Network System (MURNInet) will also be taken into account. The city council must have the industrial centers, financial institutions as well as business and trade facilities in order to attract foreign investment. Emphasis is given to the rapid development of the services sector and urban economic activities of value-adding and knowledge-orientation. The city council must have an education center complete with a university, college, colleges, museums and public libraries as well as a center for cultural activities, sporting events and leisure and conventions at the national and international level. In addition, the city council must be equipped with sufficient infrastructure facilities, adequate public utilities, etc. that are user-friendly to persons with disabilities (PWDs).

In contrast, the municipal council is a major city or administrative centre for any state or district, with a population of not less than 150,000 people and annual revenue not less than RM20 million. The municipal council must provide services at a reasonable level and sustain a good quality of life. The city council must have the industrial, business, tourism and major housing activities that have the potential to contribute to increased tax revenues as well as generating employment opportunities. It must be able to provide space and opportunities to traders as well as encourage the growth of investment, business and commercial activities. Furthermore it should have adequate infrastructure facilities and must encourage the concept of sustainable urban planning to provide safe and comfortable living conditions. Finally, the municipal council must have a program.
that encourages local people to develop their communities through efficient town management by implementing the Local Agenda 21 program or involving residents' committees.

District councils on the other hand are areas with populations less than 150,000 people and annual revenues of less than RM20 million. The district council focuses more on the communities’ needs regarding infrastructure and public utilities.
Table 2.3: Category of Malaysian Local Authorities

<table>
<thead>
<tr>
<th>Criteria</th>
<th>City Council</th>
<th>Municipal Council</th>
<th>District Council</th>
</tr>
</thead>
<tbody>
<tr>
<td>Area</td>
<td>• The administrative centre of a state.</td>
<td>• Major cities or central administration of a state or province.</td>
<td>• Other areas that are not major cities.</td>
</tr>
<tr>
<td>Population</td>
<td>• More than 500,000 people.</td>
<td>• Not less than 150,000 people.</td>
<td>• Less than 150,000 people.</td>
</tr>
<tr>
<td>Income</td>
<td>• Fiscally sustainable financial resources.</td>
<td>• Sustainable financial resources.</td>
<td>• Annual revenue less than RM20 million.</td>
</tr>
<tr>
<td></td>
<td>• Annual revenue not less than RM 100 million.</td>
<td>• Annual revenue not less than RM 20 million.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Able to balance expenditure.</td>
<td>• Provide a proper and comfortable level of services.</td>
<td></td>
</tr>
<tr>
<td>Services</td>
<td>• Able to provide high level of services.</td>
<td>• Provide space and opportunities to the traders.</td>
<td>• More focused on infrastructure and public utilities.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Encourage the growth of investment, business and commercial activities.</td>
<td></td>
</tr>
<tr>
<td>Development</td>
<td>• Emphasis on sustainable development.</td>
<td>• Emphasis on Sustainable town planning which can provide a safe and comfortable place to live.</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>• Focus on efforts to address urban issues such as squatters, illegal factories operating, safety, housing for lower income groups and the environment.</td>
<td>• Sustainable urban indicators, as emphasized in the System Malaysia Urban Indicator Network (MURNNet).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Sustainable urban indicators, as emphasized in the System Malaysia Urban Indicator Network (MURNNet).</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other Facilities</td>
<td>• Have industrial centre and financial institutions.</td>
<td>• Encourage the communities to develop efficient town management through the implementation of Local Agenda 21 program (LA 21).</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>• Good centres for education, cultural, sports and recreation activities.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Equipped with infrastructure facilities, public utilities, including public parks, and user-friendly to persons with disabilities (PWDs).</td>
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<td>• special recognition of either national or international level.</td>
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Source: Ministry of Housing and Local Government, 2008
2.4 The Management of Local Government

In Malaysia, city councils are led by mayors, while municipal and district councils are led by presidents. Prior to 1965, the mayor and members of councils were elected by local residents. However, as stated earlier, the internal administrative and political problems facing local governments and the violent confrontation against the newly-formed Malaysian Federation by Indonesia in 1964 (UNESCAP, 1999), led to the suspension of the electoral system which was replaced by a “bureaucratic dominant type of local government” (Cheema and Hussein, 1978, p.580). Following the 1965 suspension of local government, the nominative representation system was introduced (Phang, 2008a). Under this system, the state governments, elected every five years, appoint mayors, presidents and all councillors on a three-year term with the option of re-appointment (Act 171, Section 10) and in most cases come from the ruling coalition (Phang, 2008a). The Local Government Act (1976) provides for the appointment of not less than eight and not more than twenty-four councillors and a mayor or a president to sit on the full council of a local authority. Executive powers lie with the mayor in the city councils, and with presidents in the municipal and district councils. The mayor or president is supported and/or overseen by a system of committees (Phang, 2008a).

Section 10 of The Local Government Act 1976 defines the mayor or president as a member of the appointed council. The mayors in the city or presidents in the municipal councils are appointed on a full-time basis. However, in most district councils, the secretary serves full-time while the post of president is part-time (Kuppusamy, 2008). Further, Kuppusamy (2008) states that the manner in which the mayors or presidents are appointed by the state governments differs from state to state. For example, in the former Unfederated Malay States (Johor, Kedah, Kelantan and Terengganu), they are rotated among the state civil servants, whereas in other states they are appointed from among the federal civil servants.

The mayor or president has substantial influence on how the local authority is to be run and he is answerable to the state government (Kuppusamy, 2008). The mayor or president is effectively the head of council, comprised of 8 to as many as 24 members appointed by the state government. He establishes a number of committees with selected councillors serving as a members, presides over council meetings, policy-
making and other business (Haidar, Hai & Pullin, 2004). Decisions are normally made at the committee level before these are brought forward to the full council meeting generally for endorsement (Kuppusamy, 2008). However, Section 10(7) states that if the mayor or president does not agree with the other councillors on certain decisions, he/she can refer the matters to the Chief Minister or the ‘Menteri Besar’ of the state whose decision are final and binding on the local authority.

The councillors normally sit on various committees established to help the local government in management and decision-making. The number of committees depends on local governments’ planning as well as the development plan (Setapa & Lin, 2003). Section 10 of Act 171 stipulates that their selection should represent professions or the ethnic populace under the local authority. In order to carry out their duties, councillors receive allowances that may include: (i) a fixed monthly allowance, (ii) a fixed allowance plus sitting allowance subject to a certain maximum amount, or (iii) a sitting allowance only (Kuppusamy, 2008). Concerning their functions, they make policies and other decisions following recommendations from various committees and are key decision-makers in the appointment of senior council officers and their subsequent employment conditions (Haidar et al., 2004). Another important person in the MLAs is the council secretary who reports to the president, and is the chief administrative officer of municipal and district councils. In the case of city councils, a similar role is carried out by the Director-General. The secretary oversees the operations of various council departments of the local authority (Kuppusamy, 2008). He is directly responsible for implementing the policy decisions made by the council through department heads who report to him.

2.5 The Functions of Local Government

In the Malaysian federal system, the jurisdictional ability of a local government is very limited, eroded by the ultra-vires principle in the Federal Constitution. The Constitution stipulates that a local government can only perform those functions enumerated in its statutes and only within its jurisdiction (Setapa, 2003). Local Government Act 1976 (Act 171); Town and Country Planning Act 1976 (Act 172) and Street, Drainage and Building Act 1974 (Act 133) must therefore be utilized to their fullest capacity. In spite of this limitation, local authorities have been given wide powers within the Local
Government Act 1976, which provides them with a very compressive set of functions and responsibilities. Local governments operate as semi-autonomous entities within the state government framework (Tooley et al., 2010a) and perform not only mandatory functions but discretionary functions as well (UNESCAP, 1999). These functions include the following (Kuppusamy, 2008; Tooley et al., 2010a; UNESCAP, 1999):

- Collection and disposal of solid wastes;
- Providing health services, food quality control, cleanliness of food centres and control of contagious diseases;
- Provision of street lighting;
- Providing and maintaining public amenities such as wet markets, business centres stalls, sports complexes, bus stops, halls and libraries;
- Managing traffic systems and public transportation;
- Planning and overseeing development, including the preparation of structural plans;
- Licensing and control over trade, hawkers and entertainment night spots, advertising and billboards;
- Landscaping and city beautification;
- Constructing and regulating road systems; and
- Regulating drainage systems and maintaining a clean environment.

Due to financial constraints, some of the services previously were under the responsibility of local government have been taken over by the federal and the state governments (Kuppusamy, 2008). These include fire-fighting services (Fire and Preventive Services Department); the management of rivers (Drainage and Irrigations Department); drug controls and weighing scales enforcement (Ministry of Domestic Trade and Consumers); public libraries (state government); museums (Museum and Antiquities Department); water supplies and reservoir maintenance respective state water authorities, Public Works Department and Drainage and Irrigation Department); abattoir services (Veterinary Services Department); solid waste disposal (concessionaires appointed by the federal government); sewerage services, privatized in 1993 as has also been the maintenance of federal and state roads.

Although MLAs are facing financial constraints and some of the services previously were the responsibility of local government and taken over by the federal and the state
governments, MLAs are still important, as they constitute a significant component of contemporary economies and contribute greatly to the quality of life of the residents in local communities. Globally, local government is recognised as the best placed to help tackle problems of not only the community but also the national problems such as poverty, crime, climate change, migration and many other issues (Phang, 2008b). According to Abdullah and Kalianan (2008), 50% of the Gross Domestic Product is generated from local authorities’ areas. Urban population in Malaysia increased from 14.57 million or 62.0 per cent of total population in 2000 to 16.85 million or 63.0 per cent of total population in 2005 and this figure is forecasted to reach 18.47 million or 63.8 per cent of total population by 2010 (Ninth Malaysia Plan, 2006, p.361). Most, if not all, urban citizens live in local authority administered areas (Abdullah & Kalianan, 2008). Clearly, this figure indicates an urgent need for the local authorities to have sufficient abilities to face these future challenges.

The rate of urbanisation tends to correlate directly with economic growth (UNESCAP, 1999). As the population becomes urbanized, MLAs need to play their role to the optimum. The rapid increase of urbanisation in major urban centres is one direct contributor to the deteriorating local government function (Setapa, 2003) and this has created a new set of challenges where MLAs’ functions should be improved. It has resulted in the increased demand for adequate and efficient of infrastructure and public facilities (Salleh & Siong, 2008) and subsequently requires higher expenditure for extending basic facilities such as housing, roads, and transportation and healthcare facilities.

In that sense, MLAs must be prepared for modifications in meeting new challenges related to growing demands and developments. As suggested by Setapa (2003), local authorities need to change how they operate; from one of giving directives to that of a more community-envisioned or community-based analysis in the development of an action plan. By holding this principle, it is believed that the MLAs will get strong public support which will enable them to mobilise community-wide resources. In line with this, the concepts of transparency and good governance should be encouraged by which the process of policy formulation and implementation moves through consensus-building that involves all citizens. Applying concept is believed to uplift the reputation
of local authorities in the public eye and will make them more willing to contribute to taxes (Setapa, 2003).

### 2.6 The Position of Malaysian Local Government

The framework of the relationship between the three levels of government is outlined in the Malaysian Federation Constitution. By virtue of items 4 and 5 of the Ninth Schedule of the federal constitution, local government outside the federal territories of Kuala Lumpur, Putrajaya, and Labuan, is subject under the state list. All local authorities outside the federal territories therefore come under the exclusive jurisdiction of each state. By virtue of this, the state government has wide legislative powers to control the local authorities and to ensure their proper functioning.

Although the Federal Constitution provides that the organization of local government and most of the municipal services be the responsibility of the state government, it does provide for a certain degree of influence by the Federal Government through the NCLG set up under Article 95 (A) of the Federal Constitution. The NCLG can formulate policies and advise on matters pertaining to local government, and all states, with the exception of Sabah and Sarawak, need to comply with these directives (Phang, 2008b). Section 95A of the Federal Constitution provides that after consultation with state governments the NCLG can “formulate policies for the promotion, development, control of local government throughout the federation and for the administration of any laws relating thereto”. On the whole, the NCLG’s position at the central level is to ensure uniformity of and compliance with policies and rules pertaining to local government.

Figure 2.1 shows the relationship between local authorities and the federal and state governments. The powers of the state government include approval of local authorities’ budgets, appointment and removal of mayor and/or members of council, power to withhold confirmation of by-laws and the imposition of rates (Cheema & Hussein, 1978). The accountability structure between local authorities and state government is both direct and formal (Tooley et al., 2010a). Under The Local Government Act (Section 9), the state government is empowered to issue directions of a general nature to a local authority, through the mayor (president), on the policy to be followed in the
exercise of powers and duties. Bound by directives issued by state government and entrusted with resources transferred and/or authorized by state government, the formal accountability is completed by the local authorities furnishing its state government with a statement of account on their properties and activities (Faruqi, 2001). To date, the state governments through the office of the Chief Minister (Menteri Besar) can still strongly influence and control their local authorities in matters pertaining to appointment of councillors, finance, licensing, contract and project approvals (Phang, 2008b). As long as the policies at the state and local governments are in line with those of the central government, there is no justification for the federal government to intervene in matters which are considered state prerogatives.

In the past, the relationship between state and local government was problematic and left many of their local authorities in perpetual financial difficulties (Phang, 2008a). This has ultimately required the interventions of the federal government whenever the occasion demanded especially in financial and political matters. This intervention further enabled the central government to enforce its control over local government and resulted in further encroaching on its autonomy (Phang, 2008b). Under the Local Government Act 1976, the federal MHLG is responsible for implementing laws relating to local government policy in Peninsular Malaysia. The federal MHLG handles dealings between the local authority and federal government. The ministry provides advice to local authorities in matters especially related to legal and major policy issues. Although MHLG also oversees local government affairs, its influence is exerted only through its financial grants to the local authorities (Kuppusamy, 2008). These grants have to be channelled through the state government according to the State Grants (Maintenance of Local Authorities) Act 1981 (also known Act 245). Section 3 of this Act states that the federal government can impose terms and conditions on state and local governments on the use of grants provided for designated purposes. However, there is no direct control of the Ministry over local governments as they are only answerable to their state government (Kuppusamy, 2008).
Figure 2.1: The Relationship between Local Authorities and the Federal and State Government

Federal influence is also exercised through the NCLG, which was established in 1960 to ensure uniformity of local government laws and policies in Peninsular Malaysia. The NCLG acts as a forum for federal, state and local authorities to co-ordinate policies and laws relating to local authority administration as stated under Article 95A of The Federal Constitution. Chaired by the Deputy Prime Minister and the MHLG as the Secretariat, this Council is very powerful (Phang, 2008b). Its members comprise representatives of each state, usually the Chief Minister, and ten other members representing the Federal Government whereby the members meet to discuss policy matters relating to the local government at least once a year. The policy decisions made at NCLG bind both the federal and state governments (Phang, 1997). Faruqi (2001) pointed out that although the NCLG is a conduit for the transfer of federal funds to local authorities, neither it nor other federal agencies influence the financial affairs of the local authority.

Source: Cheema and Hussein, 1978, p.584; Tooley et al., 2010a, p.171.
2.7 Sources of Revenue

The general provisions for the revenue of a local authority are clearly stated under Part 5, Section 39 of the Local Government Act 1976 for those in Peninsular Malaysia, while the States of Sabah and Sarawak are governed by their respective Ordinances; in Sabah it is the Local Government Ordinance 1961 (LGO 1961, S.55) and for Sarawak it is the Local Authority Ordinance 1948 (Chapter 117) vol. 5 of Sarawak Law; the Local Authority (Rating) Regulations, the Kuching Municipal Ordinances 1988 (modification of Cap. 116/1948) and the City of Kuching North Ordinance 1988. In brief, local government revenues can be obtained from local sources such as taxes, rates, rents, fees, fines, user charges, cess, dividends from investments and incomes from any of its properties (Phang, 1997). The other forms of revenue for the local authorities are grants, contributions, in aid of rates from the federal and state governments and other public authorities. Loans may also be raised but they are subject to approval by the state authority (Setapa, 2003).

The MHLG classifies the sources of income for local authorities into six types as follows (Setapa, 2003):

- assessment taxes and rates (inclusive of contribution in-aid-of rates)
- licenses
- rentals
- government grants and contributions from the federal and state (inclusive of road grants)
- car parking charges, planning fees, compounds, fines and interests
- loans (from higher government and/or financial institutions)

Local government financial sources have remained conspicuously static, with property rating (assessment taxes) still the most significant and valuable source of income (Setapa & Lin, 2003). The assessment tax or property tax is collected based on the annual rental value or the value-added (selling price) of the property. The Local Government Act sets a ceiling rate of an assessment tax of 35 per cent of annual value or 5 per cent of value-added of a holding, and its imposition is not subject to the existence of Rent Control Act (1960). So far, the authorities have imposed a rate much lower than the maximum allowed in the Act. It can be reiterated that if local authorities
were indeed to impose the maximum rating percentage allowed, this source of revenue will certainly be a significant contributory source of revenue. Yet, due to social and political implications, local authorities in Malaysia have not levied the maximum rate (Setapa, 2003). Of all the sources of revenue classified by MHLG, assessment taxes and rates are the predominant sources of income and make up approximately 60% of total income for city and municipal councils. Grants from federal and state governments average approximately 15% of total income (Setapa, 2003).

2.8 Financial Reporting in Malaysian Local Government

Tayib et al. (1999) state that historically the regulations issued under the East India Company's Charter were the first local government legislation introduced and these were followed by the Indian Legislation Act and the Municipal Rates Act in 1848 to establish municipal committees in Penang, Malacca and Singapore (also known as the United Settlement). It was The Municipal Rates Act 1848 which provide the avenue for the public to scrutinize financial accounts, the use of public funds and the function of the committees (Kuppusamy, 2008). Under Section 15 of the (East India) Act IX of 1848, otherwise known as Municipal Rates Act, the Municipal Committee was required to publish a statement of accounts for the interest of ratepayers (Athi Nahappan Report, 1970, p. 13). This replicated similar provisions in the British Municipal Corporation Act 1835 (Coombs & Tayib, 1999). Thus, the ratepayers had the right to examine and enquire as to whether the municipal funds were being fairly and properly spent as early as in 1848.

However, there were no clear rules and regulations on the form and content of the statement of accounts that should be prepared by the MLAs were issued either before or after the independence of Malaya (Tayib et al., 1999), as shown by the following statement in the Athi Nahappan Report (1970):

It was evident to us that there exists a very grave need for a complete review of the existing accounting procedures and for the drafting of uniform model accounting procedures for adoption by all local authorities. Items of revenue and expenditure should be categorised under proper headings so that not only would it provide a clear and comprehensive picture of the financial position of
the authority but also facilitate comparative studies in local government finance (p. 253).

It is also acknowledged that the early statements of accounts prepared by MLAs are revenue and expenditure statements (Athi Nahappan Report, 1970). Even though not all suggestions mooted by this report were accepted, its finding paved the way for the restructuring of the local government system through the Local Government (Temporary Provisions) Act 1973. Following the passage of this statute in Peninsular Malaysia, all the basic laws that regulated the powers, duties, responsibilities and functions of MLAs were reviewed and codified. Tayib et al. (1999) noted that Act 171 is the most important instrument for accounting purposes as it outlines the requirement for MLAs to keep proper records and books of account. Part V of the Act 171 provides the General Financial Provisions of MLAs, while Part VI provides details regarding Accounts and Audit of MLAs. The Act 171 (for example, under sections 53 and 54) requires MLAs to keep proper records and books of account and that the annual financial report should be prepared. Section 53 of the act, for example, states that:

The local authority shall cause proper books and accounts to be provided and true and regular records to be entered therein of all transactions of the local authority and such books and accounts shall be open at all reasonable times and for reasonable periods to the inspection of any Councillor with the prior consent of the Mayor or President.

Even though the statute (for example, under sections 53 and 54) requires MLAs to keep proper records and books of account, etc., it does not make clear direction and explanation on the potential form and content of these accounts and “what consists of proper practice in compiling, or keeping the records for, as well as the financial statements under-pinning these reports” (Tayib et al., 1999, p.108). Instead, section 54 gives authority to the state governments to determine the form and content of the reports. Although Tayib et al. (1999) recommended that proper requirements or standards for MLA financial reporting should be considered by the monitoring agency, the state authorities have yet to announce any guidelines (Tooley et al., 2010b).

According to Coombs and Tayib (1999), there are no specific financial reporting requirements, either statutory or non-statutory, currently imposed on MLAs in preparing their annual financial accounts, particularly pertaining to the form and content of their financial reports. Despite the limited rules and regulations on the form and content of
the statement of accounts, Tayib et al. (1999) revealed that at least four different accounting standards have been adopted and used by MLAs. They are International Accounting Standards (IAS), guidance issued by the Ministry of Housing and Local Government (GMHLG), the FTC, and Self Created Accounting Practices (SCAP). Of these, Tayib et al. (1999) asserted that the methods advised by the FTC received the greatest priority by accountants in MLAs. The basic reason for this is that MLAs are government agencies and the annual financial accounts are mainly audited by the government Auditor General (thereafter, AG) who makes extensive use of the FTC guidance. However, there is no statutory or non-statutory provision stating that local authorities should adopt the above guidance in preparing their financial reports and accounts.

With respect to the publication of financial statements, Coombs and Tayib (1999) state that MLAs’ financial statements are not made available to the general public or council taxpayers as there is no such requirement under current Malaysian law. Financial accounts are made available to councillors, the external auditor, the MHLG and the state authority. They are eventually published in the official government gazette after audit by which the time period of the process depends on the speed with which authorities prepare their annual accounts.


Currently, federal statutory bodies, covered by the Statutory Bodies Act (Annual Report and Accounts) 1980 are adopting Federal Treasury Circular No. 4, 2007 – Guidance for preparing and Presenting Annual Reports and Financial Statements for Federal Statutory Bodies, in preparing their financial reports and accounts. These rules and regulations were developed internally by the federal government and can be regarded as self-generated accounting principles. In this circular, all federal statutory bodies are required to use accounting standards issued by the Malaysian Accounting Standards Board (MASB), either Financial Reporting Standards (FRS) or Private Entity Reporting Standards (PERS). FRS is for businesses such as publicly listed companies, their
subsidiaries, associates, or companies jointly controlled by them while PERS refer to private entities.

The purpose of the FTC is “to provide guidance for statutory bodies in the process of preparing financial accounts for publication by outlining the minimum disclosure requirements before submission to the ministry concerned” (FTC, No. 4, 2007). The circular explains the importance of accounting concepts, basic objectives and quality standards to be achieved in complying with the requirements of the user; the sole user envisaged being the Malaysian Parliament (Section II of the FTC). Paragraph 8 of the FTC requires all Federal Statutory Bodies to use accounting standards issued by the MASB, either FRSs or PERSs in preparing their annual financial statements. It also states that all accounting books and records must be kept according to the generally accepted accounting principles (GAAP) as defined in the FTC in order to ensure a true and fair view of the organisation's financial position and transactions. Paragraph 11 of the FTC defines GAAP as including accounting principles and practices which are recognised by the Malaysian professional bodies such as the Malaysian Institute of Accountants (MIA) and the Malaysian Association of Certified Public Accountants (MACPA). In the case of conflict between accounting standards and legal provisions, statute has precedence (Tayib et al., 1999). The FTC requires the following statements to be included in the annual financial accounts of government bodies (Paragraph 10):

2. Profit and loss account or income and expenditure statement.
4. Sources and application fund statement or cash flow statement.
5. Note to the account.
6. Letter of verification from the president or chairman, finance director or person responsible for the financial affairs of the body and the auditor report.
7. Other statements (specific to the body being regulated), if any.

Coombs and Tayib (1999) noted that some MLAs are adopting the MACPA’s format in presenting their annual financial statements, especially those whose statements are audited by private sector auditing firms.
Tayib et al. (1999) state that “it is claimed that by compliance with these requirements, the MLAs have shown proper stewardship of public monies and also demonstrated the ability to manage affairs and resources efficiently and effectively in achieving their policies” (p.110). Therefore, it is argued that by complying with these accounting regulations, the needs and interests of the users have effectively been taken care of. However, Tayib et al. (1999) questioned the appropriateness of application of FTC in MLAs. They argued that, unlike other government agencies, the nature of MLA activities and the needs of users of MLA published financial information cannot be directly related to the activities and the needs of users of government agencies. Therefore they suggested that there should be specific rules and regulations to govern the published accounts of MLAs. To develop the required statutory guidance expertise is needed. However, Coombs and Tayib (1999) state that attracting qualified accountants at the state level is a major problem for MLAs. Even the preparation of financial statements in some local authorities which operate without accountants is allowed in the form of contracting out the process to private sector accounting firms. Therefore these issues remain unsolved in the MLAs.
2.9 Chapter Summary

In Malaysia, despite criticisms (for example, inefficiency, lack of flexibility, lack of accountability, poor performance, too much bureaucracy and corruption) from the public, local government is still relevant and it has contributed to the growth and development of the nation. Local government represents the third tier of government in a three-tier hierarchy and has its own legal status as provided by the Federal Constitution.

In the area of inter-governmental relationships, although local government is a state matter, through the NCLG set up under Article 95 (A) of the Federal Constitution, federal government powers are exercised over local government. The NCLG can formulate policies and advise on matters pertaining to local government and all states need to comply with these directive. Thus far, the state governments through the office of Chief Minister are still in a strong position to influence and control their local government. In terms of sources of income, The Ministry of Housing and Local Government classifies them into six main groups, these being assessment taxes and rates, licenses, rentals, government grants and contributions from the federal and state, car parking charges, planning fees, compounds, fines and interests and loans.

On the issue of Malaysian local government financial reporting, there are no specific financial reporting requirements, either statutory or non-statutory, currently imposed on MLAs. The current general statutory requirements for reporting are outlined in the Local Government Act 1976, which does not clearly explain to MLAs the form and content of their financial accounts. This chapter has revealed that although the FTC is referred to by a number of MLAs in the preparation and presentation of their financial statements and annual reports, it is not a statutory requirement. It is therefore to be expected that the disclosure and reporting environments in MLA provide a particularly fruitful insight in which to study the antecedents and issues influencing financial disclosure.
CHAPTER THREE
LITERATURE REVIEW

3.0 Introduction

This chapter reviews the literature on financial disclosure studies both in the private and public sector. It is imperative to note that there is a dearth of studies related to who makes financial disclosure decisions and how they are made, how and why organization disclose their financial information, as well as institutional and social factors that influence such decisions and how these factors influence decisions in previous studies. This is particularly important from the (public sector) preparer’s perspective. This chapter is organized in four parts. The first provides an overview of financial disclosure studies. The second part reviews the managers’ disclosure decision. The third part reviews the disclosure studies in the private sector. The fourth part reviews and discusses the disclosure studies in the public sector.

3.1 Overview of Financial Disclosure

There has been an increased interest in accounting disclosure studies since the 1960s. Work by Healy and Palepu (2001), Core (2001), Beyer, Cohen, Lys and Walther (2010) and Berger (2011) provides a broad overview of the empirical disclosure literature. The literature on accounting disclosure is vast and studies have been carried out on a wide range of issues in the private and public sector as well as in developed and developing countries. Gibbins et al. (1990) defined financial disclosure as “any deliberate release of financial information, whether numerical or qualitative, required or voluntary, or via formal or informal channels” (p.122). Healy and Palepu (2001) and Beyer et al. (2010) stated that the sources of financial information can be provided through regulated financial reports (e.g. financial statements, footnotes, management discussion and analysis and other regulatory filings), voluntary communication (e.g. management forecasts, analysts’ presentations and conference calls, press releases, internet sites and other corporate reports) and disclosure by information intermediaries (financial analyst, industry expert and the financial press).
The credibility of the information disclosed can be enhanced by regulators, standard setters, auditors and other market intermediaries (Healy & Palepu, 2001). In general, financial disclosure can be divided into two broad categories: mandatory disclosure and voluntary disclosure. Mandatory disclosure is information disclosed in the fulfilment of disclosure requirements either it is by legislation in the form of laws, professional regulations in the form of accounting standards and the listing rules of stock exchanges requirements. Voluntary disclosure is regarded as any information disclosed in excess of mandatory requirements.

Financial disclosures by management are the primary methods of keeping stakeholders informed about organization performance. Disclosures of financial information are a means of communicating a firm’s financial performance to outside stakeholders. Beyer et al. (2010) state that the financial information serves two important roles in capital market economies. First, it is related to the valuation role of accounting information whereby investors or capital provider can evaluate the return potential of investment opportunities. Second, it is related to the stewardship role of accounting information whereby investors are allowed to monitor the use of their capital once committed. Thus, the demand for accounting information by the outsiders (especially investors) arises for two reasons (Beyer et al., 2010; Healy & Palepu, 2001). First, a firm’s managers typically have better information than outsiders about the value of both firms’ current and future business investments and these managers have incentives to overstate their value. If the outsiders are not able to assess the firms’ value or profitability, the capital market tends to undervalue good investment opportunities and overvalue bad investment ideas, which potentially lead to market failure. The outsiders, therefore face an information or lemon problem; the situation where the outsiders and managers have conflicting information and incentives. Secondly, demand for the accounting information arises due to a separation of ownership and control which results in investors not having full decision-making rights (Beyer et al., 2011). Healy and Palepu (2001) argue that, once the investors invested their funds in business ventures, self-interested managers have an incentive to make decisions that expropriate investors’ funds, thus creating an agency problem. Therefore, demand for financial disclosure arises from information asymmetry and agency conflict between managers and outside investors.
Many solutions to information and agency problems\(^4\) have been suggested including contacting, disclosure, regulation, information intermediaries (Healy & Palepu, 2001). A variety of economic and institutional factors have been tested to determine their effectiveness. On this theme, many empirical studies have been conducted on financial reporting and disclosure and most are primarily focused on the cross-sectional variation of economic and institutional factors or variables to explain management’s financial disclosure decisions (Healy & Palepu, 2001). The following section discusses the motivations and incentives for accounting choices and voluntary disclosures.

3.2 Manag**ers’ Disclosure Decisions**

Research regarding managers’ disclosure decisions can be classified into two main areas (Healy & Palepu, 2001). The first area is mainly focused on management financial reporting choices where the central issue is to examine the role of contracting and political considerations in explaining management accounting choices when there are agency costs and information asymmetry. Fields, Lys and Vincent (2001) identified three motivations for accounting choice. First, the accounting choice is said to influence the firm’s contractual arrangements. The second motivation is driven by information asymmetries in the attempt to influence asset prices. The primary focus is “to overcome problems that arise when markets do not perfectly aggregate individually held information” (p.262). Finally, managers hope to influence the decisions of third parties by choosing appropriate reporting regulations and standards.

The second area is on voluntary disclosure which mainly focused on management disclosure decisions and concern on the information role of financial disclosure for capital markets. The available literature has suggested many ways in which a firm or its management can benefit from disclosure. Therefore, the firm’s disclosure decisions are likely to be motivated by a variety of incentives. Healy and Palepu (2001) and Beyer et al. (2010) discuss six incentives for voluntary disclosure identified in the disclosure studies literature. These six incentives are described in more detail as follows:

- Capital market transactions. In order to reduce the information asymmetry problem, managers who anticipate making capital market transactions have incentives to provide voluntary disclosure and thereby reduce the firm’s cost of

\(^4\) Beyer et al. (2010) termed these as valuation and stewardship problems respectively.
external financing. Iatridis (2008) found that in order to raise capital and debt markets, firms tend to provide extensive accounting disclosure.

- Corporate control contests. The managers are held accountable for stock performance by boards of directors and investors. Given they risk losing their jobs if poor stock and earnings performance occur, managers use disclosures to reduce the likelihood of undervaluation and to explain away poor earnings performance.

- Stock compensation. Managers who are rewarded using a variety of stock-based compensation plans (e.g. stock option grants and stock appreciation rights) have incentives to engage in voluntary disclosures.

- Litigation costs (e.g. Skinner, 1994). This stems from the threat of shareholder litigation. The threat of shareholder litigation can have two effects on managers’ disclosure decisions. First, legal actions against managers for inadequate or untimely disclosures can encourage firms to increase voluntary disclosure. Secondly, litigation can potentially reduce managers’ incentives to provide disclosure, particularly of forward-looking information.

- Proprietary costs. Firms’ decisions to disclose information to investors is influenced by concern that such disclosures can damage their competitive position in product markets. Firms have an incentive not to disclose information that will reduce their competitive position, even if it makes it more costly to raise additional equity.

- Management talent signaling. In order to reveal their type, managers with talent have an incentive to make voluntary disclosures.

To sum up, accounting choice and the disclosure of any information in excess of mandatory requirements of managers are driven by several motivations and incentives. These incentives and motivations are discussed further in the literature review on disclosure studies in the following section.
3.3 Disclosure Studies

According to Beyer et al. (2010), many approaches are used in the literature to study the concept of disclosure. These approaches include survey ranking (based on questionnaire forms), researcher-constructed indices, natural language processing techniques and properties of a firm’s reported earnings analysis. For this thesis, these studies are broadly categorized into three significantly different approaches, namely researcher constructed indices, field-based research and survey ranking. Here disclosure studies are divided into those in the private sector and those in the public sector. The disclosure studies in the private sector are discussed first.

3.3.1 Disclosure Studies in the Private Sector - Researcher Constructed Disclosure Index

Voluminous studies have been carried out to explain the level of disclosure as well as to measure the disclosure and reporting quality. Researcher constructed indices have dominated disclosure studies in the private sector. These studies address the association between a constructed disclosure index of mandatory, voluntary or total accounting disclosure and certain firm, corporate governance and cultural characteristics. More specifically, many researchers have taken an interest in firm characteristics that could predict a business’s disclosure level. It is worth noting the fact that many firms have provided voluntary disclosures – disclosures that exceed the disclosure requirements and provide additional information not specifically required by the existing law or accounting standards (Chavent, et al., 2006). As a consequence, voluntary disclosures have become the focus of increasing attention by accounting researchers (see for example, Cooke, 1989; Wallace, Naser & Mora, 1994; Meek, Roberts & Gray, 1995; Ahmed, 1996; Inchausti, 1997; Owusu-Ansah, 1998; Depeors, 2000; Richardson & Welker, 2001; Haniffa & Cooke, 2002; Ferguson, Lam & Lee, 2002; Eng & Mak, 2003; Prencipe, 2004; Cahan, Rahman & Perera, 2005; Chavent et al., 2006; Alsaied, 2006; Mohd-Ghazali & Weetman, 2006; Iatridis, 2008; Wang et al., 2008; Hossain & Hammami, 2009).

Within these disclosure studies, many factors or characteristics leading entities to disclose information have been studied. The majority of disclosure studies have focused
on corporate characteristics, such as firm size (Buzby, 1975; Hossain et al., 1995; Hossain & Adams, 1995; Depoers, 2000; Cahan, Rahman & Perera, 2005; Chavent et al., 2006; Alsaeed, 2006; Iatridis, 2008; Wang et al., 2008; Hossain & Hammami, 2009), audit firm status (Hossain & Adams, 1995; Inchausti, 1997; Ahmed, 1996; Wang et al., 2008), & firm age (Hossain & Hammami, 2009). All of these factors have been examined and found to be associated with firms’ disclosure level.

For example, in Malaysia, Haniffa and Cooke (2002) studied numerous and extensive variables in order to explain the extent of voluntary disclosure. In addition to firm-specific characteristics, they included a number of corporate governance and cultural characteristics to examine their relationships with the extent of voluntary disclosure in the annual reports of Malaysian listed corporations. They constructed an unweighted disclosure index that consists of 65 voluntary disclosure items. The study found a significant link between two corporate governance variables (chairperson who is a non-executive director and domination of family members on boards) and the extent of voluntary disclosure. In addition, one cultural variable (proportion of Malay directors on the board) is significantly associated with the extent of voluntary disclosure. Four firm-specific characteristics (assets-in-place, top ten shareholder, foreign investors and profitability) were found to be significantly associated with the extent of voluntary disclosure in this study.

Another Malaysian study of listed firms conducted by Akhtaruddin, Hossain, Hossain, and Yao (2009) investigated the extent of corporate governance factors (board size, proportion of independent non-executive directors (INDs) on a board, outside share ownership, family control, and percentage of audit committee members to total members on the board) and voluntary disclosure. The authors found a positive association between board size and proportion of INDs and voluntary disclosures.

Thus many firm, corporate governance and cultural characteristics have emerged as influencing the disclosure level of the organization. Most disclosure studies have employed conventional statistical methods to test empirical hypotheses. The common method used is to construct a firm-based disclosure index and to relate the extent or quantity of informational items disclosed to various related firm characteristics (Ahmed & Courtis, 1999, Chavent et al., 2006; Alsaeed, 2006). The index comprises voluntary
and/or mandatory information items depending on the research objective and the country being examined (Ahmed & Courtis, 1999).

The previous financial disclosure studies have however, been subjected to several criticisms. Using the conventional statistical method in disclosure studies has been openly criticised by Watt and Zimmerman (1986, cited in Adams, 1997), who argued that “the use of statistical methods has often produced inconclusive and counter-intuitive results” (p. 718). There are several reasons for such criticism including the application of imprecise proxies, different sample sizes, inadequate sampling methods, mis-specified functional models (Watt & Zimmerman, 1986) as well as differences in research settings, disclosure index construction and definition of the explanatory variables (Ahmed & Courtis, 1999). Chavent et al. (2006) argue that there are several limitations to the common methodological approach employed in disclosure studies. First, there is no one dominant practice on the use of disclosure index. Second, including too many variables may create a multicollinearity difficulty and third, the form of relationship between dependent and independent variables is not always known. Furthermore, Alsaeed (2006) criticizes the definition of the quality of disclosure in the studies because it has not been firmly defined. For example, Buzby (1974) used the term adequacy, Wallace, Naser and Mora (1994) used the term comprehensiveness, and Iatridis (2008) used the term extent. In addition, Healy and Palepu (2001) and Beyer et al. (2010) argue that the findings from self-constructed indices are difficult to be replicated and generalised because a construction of such matrices involves the researcher’s subjective judgement. Moreover, constructing the measures that rely only on disclosures provided in the firm’s financial statements and other public forums and documents may not capture the disclosures that firms provide during conference calls and other related venues that might complement or substitute for the information in financial statements. The following section reviews the financial disclosure studies conducted using the method of field research.
3.3.2 Disclosure Studies - Field Research

Only a few studies have conducted field research to study accounting disclosure (for example, Gibbins et al., 1990; Holland & Stoner, 1996; Adams, 1997; Holland, 2005). Unlike the management accounting field, field research studies are still not a popular method for financial disclosure in financial accounting (Holland, 2005; Merchant & Van de Stede, 2006; Cooper & Morgan, 2008).

Gibbins et al. (1990) took a different approach in studying accounting disclosure. In their field-based study of disclosure practices, they analysed the transcripts of 20 interviewed people involved in the disclosure process of Canadian companies, from which they developed a model to explain organization financial disclosure. This model is an empirically derived structured designed to explain and predict a firm’s financial disclosure policy. The model posits that the financial disclosure is an array of managed activities, and according to this model the output in the disclosure process is produced in response to internal or external antecedents. The organization’s readiness to disclose is “a function of its developed disclosure position, the existence of internal or external structures for handling disclosures, and the presence of auditors, consultants, or other external mediator” (p.128). Disclosure position according to this model has a number of significant internal and external antecedents and these may affect the structure and use of external mediators and the disclosure position itself. Gibbins et al. (1990) further explain that:

> When management perceive an issue having disclosure implications, any disclosure norms and opportunities are (or may be) identified. Disclosure position, mediators and structure may influence the identification of issues and the perception of associated norms and opportunities. Then the disclosure outputs are generated as a function of the perceived norms and opportunities, the disclosure position’s ritualistic and opportunistic dimensions, and any existing structures (p.128).

Adopting a framework from the model of corporate disclosure of Gibbins et al. (1990), Adams (1997) conducted a field-based research using interview evidence collected from financial managers of 12 New Zealand-based life insurance companies to investigate the motives for voluntary disclosure. This study found that company culture was a major determinant of corporate reporting practices and managers did cite conservatism and the
traditionally strong influence of actuarial principles as influencing their reporting. Evidence of opportunism was also found in reference to the influence of dominant personalities in the reporting process. This study suggested that disclosure is a complex event, which is influenced both by organizational antecedents and environmental antecedents. Such antecedents include company culture and tradition, characteristics of the parent company, intra-organizational networks, and influence of dominant personalities and the proportion of accountants employed in the firm. Organizational antecedents include the influence of external auditor, market competition, and industry norms. This study suggests that it is possible to improve our understanding of the disclosure process by taking different views of the process and using field-based research to study complex and multi-dimensional phenomenon of corporate disclosure.

Holland and Stoner (1996) adopted a grounded theory approach to explain disclosure of price sensitive information (PSI). Their results indicate that the firm’s readiness to disclose was a function of their developed policy, the existence of a structured PSI decision process and of responsive internal and external structures for handling disclosure, the presence of internal advisers and communications specialists. Disclosure position had a number of significant internal and external antecedents. The changes in these antecedents affected internal and external structures and the use of external mediators. Thus, their findings bear similarities to Gibbins et al. (1990).

Holland (2005) also adopted the grounded theory approach to explain how companies in the UK voluntarily disclose information through private and public channels. The study showed that firms employ several disclosure channels that are public, semi-private and private in character. Public disclosure relates first to mandatory information (that is, required by company and securities law). However, additional public information is provided at the managers’ discretion, as part of their strategy of managing the communication process to achieve business objectives. The study also suggests that disclosure of information is affected by both firm and market factors, and thus bear important similarities to Gibbins et al.’s (1990) and Holland and Stoner’s (1996) studies. Further, the study asserted that the disclosure activity led to cumulative corporate learning about perceived market outcomes and their fragility. The interaction and learning fed back into cumulative corporate understandings and experiences of their disclosure behavior which then in turn became drivers of subsequent disclosure.
In summary, the studies in the field-based research consider organizational, social and environmental factors to explain the disclosure practices and management of business organizations. However, these studies are limited to the private sector and developed countries. No further studies have been conducted to test their findings to the public sector. Moreover, there is a dearth of financial disclosure literature utilising field-based research. Considering these limitations, this thesis intends to test the Gibbins et al. model to the public sector by employing field-based research.

3.4 Disclosure Studies in the Public Sector

Compared to the private sector, studies investigating disclosure practices in the public sector are limited (Laswad, Fisher & Oyelere, 2005). Some studies investigated the incentives for financial disclosure (Ingram, 1984; Luder, 1992; Cheng, 1992; Baber, 1983; Baber & Sen, 1984; Evans & Patton, 1987; Ingram & DeJong, 1987; Giroux, 1989; Christiaens, 1999; Gore, 2004). Some studies in the public sector used the survey approach by sending questionnaires to various financial accounting information users in order to identify who used financial statements. Some requested the users to rank specified accounting items according to their degree of importance for decision-making processes and why they needed such financial information (Jones, Scott, Kimbro, & Ingram, 1985; Daniel & Daniel, 1991; Alijarde, 1997; Jones & Puglisi, 1997; Tayib et al., 1999; Mignot & Dolley, 2002; Mack & Ryan, 2006).

In the public sector, financial disclosure is increasingly expected to provide stakeholders with a “true and fair” view of the entity’s performance (Borgonovi & Anessi-Pessina, 2000). Accounting disclosure should be expected to become important for decision-making process and to help us understand how the entity’s inflows, outflows, assets, liabilities, surpluses and deficits affect their own interests and expectations (Borgonovi & Anessi-Pessina, 2000). Ryan, Stanley and Nelson (2002) argue that accountability and decision usefulness are two commonly accepted objectives of public sector financial disclosure. In a similar vein, the annual report which includes both the financial and non-financial information reporting has been identified as one of the main documents available for the public sector to communicate information about its activities to stakeholders (Kloot & Martin, 2001; Hyndman & Anderson, 1995).
Tooley et al. (2010b) argue that disclosure in the accounting context is primarily concerned with the gathering of data, moulding it into a particular presentation format, and dispatching it into the substantial environment. The broader disclosure function leads to the issues of incentives for disclosure, whom to report to, what to report and why stakeholders require the information (Mack & Ryan, 2006; Tooley et al., 2010b).

The next section highlights the stream of research on the issues of incentives for disclosure, users’ identification of public sector financial reports and is followed by two sections that review studies which investigated the usefulness of the financial statements in the public sector. These include the questions of what to report and why it is required.

### 3.4.1 Incentives for Financial Disclosure

Some studies in the public sector have investigated how several factors are linked to accounting choice. Many incentives have been identified and they can be grouped into four broad categories: political incentives, social incentives, institutional or administrative incentives and economic or financial incentives (Perez, Bolivar & Hernandez, 2008). Under these four categories, previous studies have sought to analyse their influence on information disclosure. For example, under political incentives, political culture (Luder, 1992) and political competition (Cheng, 1992; Carpenter, 1991; Baber, 1983; Baber & Sen, 1984) has been examined. Most of these studies found a significant positive relationship between political incentives and disclosure. Inconsistent with the above findings, Giroux (1989) suggests that each group with political power has only limited influence on disclosure.

Under social incentives, the following have been identified as factors influencing financial disclosure: socio-economic level (Ingram, 1984), education level of voters (Ingram, 1984), size of population (Evans & Patton, 1987), public media visibility (Cheng, 1992; Laswad, Fisher & Oyelere, 2005; Gandia, 2008; Garcia & Garcia-Garcia, 2010) and the access to technology and educational levels of the citizens (Perez, Bolivar & Hernandez, 2008; Gandia, 2008).

Under institutional incentives, several studies have investigated the association between audit status and audit opinion and disclosure in the public sector (e.g. Gordon et al.,
2002; Giroux, 1989) and they found a significant relationship between these factors and disclosure. Some studies also examined the relationship between the form of local government and monitoring incentives (Evans & Patton, 1987; Ingram & DeJong, 1987; Giroux, 1989; Giroux & McLelland, 2003). In general, these studies show a positive relationship between the form of local government and disclosure choice. A number of studies examine the relationship between the size of government and monitoring behaviour (Baber, 1983; Ingram, 1984; Evans & Patton, 1987; Ingram & DeJong, 1987; Christiaens, 1999). However, these studies have reported mixed evidence. While Ingram (1984) and Evans and Patton (1987) showed no statistical association, Baber (1983), Ingram and DeJong (1987), and Christiaens (1999) reported a significant positive relationship between size and disclosure choice. With respect to the effect of regulation, while theory supports the proposition that disclosure regulation results in higher disclosure levels, municipal disclosure studies have found mixed results on such a relationship. A study by Ingram and DeJong (1987) for example, finds no significant difference in disclosure levels between GAAP-regulated and unregulated states. Ingram and Dejong (1987) investigated the reporting practices of 544 U.S. cities in order to evaluate the relationship between financial disclosures of local government and the economic incentives of the local political manager to disclose. The primary economic incentive of interest in their study was the regulatory structure of local government’s financial reporting. They found that disclosure practices of cities in states that do not regulate local government practices do not differ significantly from the practices of cities in GAAP-regulated states. This suggests that, when the political and socioeconomic situation warrants disclosure, political managers have incentives to disclose the information whether or not they are required to do so by state regulations. They further argue that state regulations result in costs to the state for monitoring and enforcement and to local governments for complying with reporting requirements and these costs appear to be unnecessary if other incentives are sufficient.

Gore (2004) investigated the effects of disclosure regulation on municipal managers’ incentives to disclose financial report information to the bond market. She compared municipal disclosure levels in a state that requires GAAP regulation with those municipal disclosure levels in a state with unregulated disclosure. She first examined disclosure in an unregulated disclosure and then examined the influence of regulation on disclosure. She found a significant positive association between disclosure levels and
proxies for bond market interaction in the unregulated state, which suggests that in the absence of regulation, municipal managers disclose financial report information because they have bond market-induced incentives to do so. Gore (2004) believes that a failure to adequately control for differences in regulatory environments and focusing only on larger municipal authorities, may explain some of the inconsistencies found in prior studies. After controlling for these factors, Gore (2004) discovered that GAAP disclosure levels were significantly higher in the regulated state than in the unregulated one, which is inconsistent with Ingram and Dejong (1987).

Finally, under economic incentives, several studies have investigated the association between the debt or cost of debt and disclosure in the public sector and provided inconclusive results. Ingram and Dejong (1987), Evans and Patton (1987), and Perez, Bolivar and Hernandez (2008) found a significant relationship between debt and disclosure in the public sector, while the studies of Baber (1983), Baber and Sen (1984), Ingram (1984) and Christiaens (1999) reported no link between debt and disclosure. Additionally, the federal/state transfer of fund emerged as significantly associated with disclosure in public sector disclosure studies (Ingram & DeJong, 1984).

To sum up, various incentives have been identified by the researchers for the accounting choice with some studies providing mixed and conflicting results. In broad terms these incentives can be grouped into four types: political incentives, social incentives, institutional or administrative incentives and economic or financial incentives. However, due to various measures of accounting disclosure used in some studies, the research findings are difficult to compare. In addition, Cheng (1992) states that “due to multicollinearity among independent variables, data reduction methods resulted in different measures being used for similar constructs in each analysis. As a result of the differences in the selection of measures for both the dependent and independent constructs, identifying specific variables that are important for explaining accounting choice has been problematic” (p. 2).
3.4.2 Disclosure Studies - Survey Ranking

Some studies were conducted based on survey ranking by sending questionnaires to various financial accounting information users and financial accounting information preparers, requesting them to rank specified accounting items according to degree of importance for decision-making processes (Buzby, 1975; Firth, 1978; Alijarde, 1997; Jones & Puglisi, 1997; Tayib et al., 1999; Mignot & Dolley, 2002; Mack & Ryan, 2006). To sum up, most of the survey ranking studies were carried out to identify the users of public sector financial reports, and to investigate the usefulness of the financial disclosure which includes the questions of what to report and why the information is required. The studies on users’ identification are discussed next.

3.4.2.1 Identification of Users of Financial Information

Prior public sector research suggests that the identification of users and their information requirements is critical to an evaluation of financial statements produced by relevant agencies. There are some studies on the actual and potential users of the public sector reporting. Some authors have used normative arguments to identify user groups or classifications (Anthony, 1978; Drebin, Chan & Ferguson, 1981; Jones, Scott, Kimbro & Ingram, 1985; Borgonovi & Anessi-Pessina, 2000). A study carried out by Anthony (1978) normatively classified users into five categories: governing bodies, investors and creditors, resource providers, oversight bodies, and constituents. He suggested that in order to be useful, the list of user groups must be brief. Mack and Ryan (2006) argue that the majority of subsequent normative work has either adopted these categories of users as a basis for further conjecture or re-classified or taken them as given and examined information needs issues.

Drebin et al. (1981) identified potential user groups based on extensive reviews of the literature and investigations of the structure of state and local government. They identified resource providers, resource allocation decision-makers, elected officials, the electorate and external parties involved in transactions with the entity as major user groups. Jones et al. (1985) examined state and local governments, identifying investors
and creditors, citizen groups, and legislative and oversight bodies as the users of financial information.

Borgonovi and Anessi-Pessina (2000) listed many local government accounting information users, classifying them as external and internal stakeholders. External stakeholders include: citizens (as consumers and taxpayers); firms and other socio-economic organisations; upper levels of government and other oversight agencies; banks, individuals and international institutions; foreign investors and country analysts; and future generations. Internal stakeholders include: institutional bodies (e.g. the cabinet and the legislature) and political groups; public managers; government employees; and public-sector trade unions as users and potential users.

These normative studies have been important in determining the direction of both normative work and empirical work. However, they have been subjected to several criticisms. Jones (1992) argued that taking certain users and certain needs, for which there is no empirical evidence, establishing the objectives of public accounting information can lead to outputs of information that are not as useful as they were expected to be. In addition, these studies cannot document the complexities and variations of the environments in which financial reports are produced in the public sector (Lapsley, 1992).

Other authors have tried to identify the actual users of public organization reporting through empirical research (Atamian & Gangguli, 1991; Alijarde, 1997; Mack & Ryan, 2007). Atamian and Ganguli (1991) conducted a study to identify the primary recipients of municipal financial reports in the USA. In order to determine whether the individual municipalities sent their reports to the user groups identified in prior research (individuals, private businesses, private non-business organisations, state and local government institutions and federal government agencies), Chief Financial Officers of all municipalities with a population of over 50,000 were surveyed. Their study revealed that not all users identified were on the mailing lists. The authors identified city employees (as internal users) as a significant category of recipients as well as other municipalities. In addition, there were recipients not identified in the literature (for example, other municipalities) which did appear on the distribution lists.
Alijarde (1997) analysed local government in Spain. Part of her study sought to determine who uses public sector financial reports. Both finance directors and audit officers claimed to be primary users. They also perceived resource providers as a major user group. However, a governing body of council, citizens and political parties were perceived as not important users of financial information. In their attempt to investigate the role and importance of the annual report as a source of information about public sector entities, Mack and Ryan (2006) directly accessed users of public sector annual reports and asked them to self-assess the nature of their relationship with three different entity types (government departments, local government authorities and government-owned corporations). They classified users into internal and external stakeholders. Internal management and elected officials were classified as internal stakeholders while ratepayer/taxpayer, other resource provider, oversight bodies, and other similar entities and recipients of services were classified as external stakeholders. They found that 29.8% of their respondents were internal management, 20.8% were oversight bodies, 20.4% were other similar entities, 13.1% were other resource provider, 8.7% were ratepayer/taxpayer, 4.8% were elected officials and 2.4% were other recipients of services.

The categories of potential users for a local government can be summarized as follows:

- **External users:**
  1. Citizens (as consumers and taxpayers/ratepayers);
  2. Firms using public services;
  3. Upper levels of government;
  4. Oversight agencies;
  5. Auditors;
  6. Other local governments;
  7. Banks and lenders;
  8. Foreign investors, analysts, rating agencies;
  9. Individuals and international institutions

- **Internal users:**
  1. Councillors and executive members;
  2. Institutional bodies (e.g. the cabinet and legislature) and political groups;
3. Public managers;
4. Government employees;
5. Public sector trade unions.

Overall empirical and normative studies have failed to reach a consensus in identifying the users of financial information in the public sector (Steccolini, 2004) and this is still the subject of ongoing debate in the public sector. Some users who have not been previously normatively identified were identified in the empirical studies. This may be due to the fact that different users will have different information needs. Specifically, individual user groups may have distinct purposes for requiring information. Thus, identifying the needs of public accounting information users has been dealt with in numerous statements and studies.

### 3.4.2.2 Information Required by Users

With respect to the usefulness of financial information, several studies have sought to determine what information users may require or what financial information they find useful seeking the views of representatives of users previously identified in the literature. An early empirical study was carried out by Robbin (1984). He sought to determine the consensus between the information needs of users of municipal annual reports and report preparers’ perceptions of user needs. Municipal bond analysts as users and municipal finance officers as preparers were surveyed on the importance they placed on information items generally included in municipal annual reports. The study concluded that preparers of financial reports understand users’ information needs. However, they generally underestimate the importance of the information they provide. The study also concluded that a moderate degree of agreement exists between preparers and external users about the relative importance of items of financial reporting. This research is important in that it showed preparers of financial reporting perceived the important needs of external users.

Jones, Scott, Kimbro, and Ingram (1985) sought the views of users of the financial reports of state and local governmental entities on the information content. The user groups involved in the study were investors and creditors, citizen groups and legislative and oversight officials. The study revealed that there were differences in the information
of interest to users. Investors and creditors were more interested in the cash flow statement while citizens were more interested in cost of services information. This analysis also found that fund-type statements were considered more useful than consolidated statements. Daniel and Daniel (1991) used the same user groups as Jones et al. (1985) in their attempt to identify any disparity amongst user groups in terms of their information needs and decision accuracy. Their study revealed that investors and creditors were most interested in information on performance and viability while legislative and oversight officials rated information on compliance and cost of services most useful and also expressed an interest in information on performance and viability. Citizen groups preferred information on cost of services (efficiency and effectiveness). The study supported the study by Jones et al. (1985) which claimed that there were differences in how users valued the usefulness of information. In addition, all users group felt that the financial statements were not sufficient to evaluate the financial condition of the municipality.

Alijarde (1997) carried out a study on the usefulness of financial reporting in Spanish local governments. Based on a survey of finance directors of local governments and audit offices, the study found that financial disclosure in local government can be useful for financial directors and public auditors. The finance directors and auditors utilised financial reports differently depending on their importance in decision-making processes. The author discovered that finance directors valued a budget execution statement as most useful, while public auditors considered the cash statement and statement of debt as the most relevant. However, both groups agreed on the high degree of usefulness of statement of debt and cash statement.

In Australia, Jones and Puglisi (1997) surveyed the preparers (senior government department officials and representatives) of government department financial reports to assess the usefulness of general purpose financial reports for decision tasks. They found a lack of support for the introduction of accrual accounting techniques. Although the techniques could benefit certain users, the respondents did not perceive general purpose of financial reports to be relevant to a wide range of users. With the same objective in mind, Mack and Ryan (2006) sought to determine the appropriateness of the general purpose financial reports model to government departments by empirically identifying users of general purpose financial reports and their information requirements. They
found that users identified performance information which includes summary facts figures and key statistics, financial overview and analysis, performance indicators and budget versus actual information as being useful for the purpose of discharging financial and public accountability. They also found that the model is mis-specified and inappropriate for the public sector with its complexity of operating structures, sources of financing, operating motives and accountability. In particular, they found that general purpose financial reports are used to satisfy financial and public accountability rather than for decision-making. This is indicative of users having an accountability focus rather than a ‘decision-useful’ focus.

In Malaysia, Tayib et al. (1999) undertook a survey of taxpayers from three local government authorities which had differing levels of tax payment arrears to investigate and explore the needs and demands of taxpayers for financial information disclosed by these local authorities. The results revealed that regardless of the level of tax arrears, taxpayers preferred income and expenditure information over both balance sheet and funds statement-type information. However, the results showed that there were significant differences in the interest of taxpayers in income and expenditure information depending on the level of taxation arrears of the authority. Taxpayers from local government authorities with higher levels of taxation arrears displayed more interest in reading all of the information items above than did those in medium and low levels of taxation arrears. With regard to taxpayers’ willingness to read financial accounts and pay local tax, the results suggested that the provision of additional relevant financial information has the potential to significantly improve the level of assessment tax collection.

Another Malaysian study by Tooley et al. (2010b) found that disclosures in the statement of revenue and expenditure and forward looking information are generally regarded as the most important disclosure. The study also found differences amongst stakeholders as to the level of importance that they place on certain items, especially items related to internal policies and governance and local authorities’ financial position.
3.4.2.3 Why Users Require Information

Several studies have investigated the reasons for which users require information. Jones et al. (1985) found that there were some differences identified in the information requirements of individual user groups. The citizen groups used financial reports for: evaluating efficiency and effectiveness, comparing results of the current year with those of previous years; assessing financial operations and financial conditions; determining compliance with the budget and advocating certain programmes. Legislative and oversight officials use governmental financial reports primarily to: evaluate executive branch funding and spending proposals (by comparing results with previous years); determine compliance with the budget and other finance-related requirements; monitor fund activity (performance) and financial position (viability) and analyse fund balances. Finally, investors and creditors use governmental financial reports to ascertain the ability of a government to repay its debt.

Alijarde (1997) found that finance directors and auditors utilised the financial reports differently. Finance directors recognised that financial reporting is useful for assessing budgetary execution and the results of the period, facilitate the accountability process, legal and financial control and is useful for decision-making. In contrast, auditors viewed it primarily from the perspective of accountability.

In Australia, two studies investigated the usefulness of general purpose financial reports for decision tasks. Firstly, Jones and Puglisi (1997) found a lack of support for the introduction of accrual accounting techniques. They argued that the techniques could be of benefit to certain users, however respondents did not perceive a general purpose of these financial reports as being relevant to a wide range of users. However, the researchers suggested that the attitudes to the relevance of accrual accounting could become more favourable once government departments begin to prepare and trial general purpose financial reports over a period of time.

Conducted in an Australian health department, Mignot and Dolley (2000) investigated whether two groups of users (legislators and interest group members) found financial statements information useful for making decisions. The lobbying tasks included activities such as writing to a newspaper, complaining to a member of Parliament,
informing others about a government activity and protesting publicly. The decision task selected for legislators was inquiries about a government department such as seeking further information about expenditure and programs. Their results showed that the legislators and citizen coalition members found accounting statement information useful for their decision tasks. Their results also demonstrated that there is no difference in the perceived usefulness of financial statements for these two groups. These results conflict with those of Jones and Puglisi (1997) regarding the usefulness of financial reports for certain user groups. In another Australian government department setting, Mack and Ryan (2006) found that financial statements information is more useful for discharging financial accountability and public accountability than decision-making. Contrary to the findings of Mignot and Dolley (2000), they did not find financial statements information to be useful for decision-making.

Overall, it can be seen that empirical investigations seeking the information needs of users have been conducted for various types of users and potential users and a number of public sector agencies. Some studies aimed to show the needs of each user group and others attempted to influence the informing organisations by highlighting the specific needs of certain user groups that they considered to be significant. The results of these empirical studies indicate that the disclosure needs of users have not been met and that different user groups have different information needs according to their interests, functions, competences and depending on the entity in which they have an interest. Some studies show that the financial disclosure can be useful for users’ decision-making processes. However, the studies also reveal the need to introduce some changes that allow information that meets different users’ needs.
3.5 Chapter Summary

The literature on accounting disclosure is enormous and studies have investigated a wide range of issues. In broad terms, the disclosure studies in the literature can be categorized into three different approaches, namely: researcher constructed indices, field-based research and survey ranking. Within the disclosure studies in the private sector, many firm, corporate governance and cultural characteristics have influenced the disclosure level of the organization. However, the majority of these studies have employed conventional statistical methods to test empirical hypotheses. Furthermore, field research studies are still not a popular method for analysing financial disclosure in financial accounting. Only a few disclosure studies in the private sector and developed countries used the field-based research method.

Within the public sector, the search for the appropriate financial disclosure model has given rise to some issues, such as who uses the financial information and why. Many incentives have been identified in relation to accounting choice and they can be grouped into four categories: political incentives, social incentives, institutional or administrative incentives and economic or financial incentives.

Prior public sector research suggests that the identification of users and their information requirements is critical to an evaluation of financial statements produced by the public sector agencies. In response to this, there are some studies on the actual and potential users of the public sector reporting. Some authors have used normative arguments to identify user groups or classifications, and others try to identify the actual users of public organisation reporting through an empirical research. Similarly, empirical investigations to determine the information needs of users have been conducted across a number of jurisdictions, across users or user groups, as well as across a number of the public sector entity types.
CHAPTER FOUR
THEORETICAL FRAMEWORK

4.0 Introduction

This chapter describes the conceptual and theoretical basis of this study. The chapter analyses the various theories used in disclosure studies, critiques these theories and then justifies the theory chosen for this study. The chapter also describes theory which is used in this study, namely the Gibbins et al. (1990) model. This chapter commences with the discussion on the role of theory in research and then proceeds to discuss the theoretical approaches to disclosure, followed by description of the important features of Gibbins et al. Model and how it is being employed in this research.

4.1 The Role of Theory in Research

Corbin and Strauss (2008) explained a theory as a “set of well developed categories that are systematically interrelated through statements of relationship to form a theoretical framework that explains a phenomena” (p.55). A number of researchers have acknowledged the potential role of theories in field-based studies. For example, Zimmerman (1987) points out that “not all data and facts can be collected and reported – the world and field sites are too complex. Some theory, underlying model, or framework always directs the researcher to those facts considered interesting or important to collect and report” (p.290). Ryan, Scapens and Theobald (2002) argue that a theory or framework used for the case study approach enables the researcher to explain convincingly the observed accounting practices. They recommend that the available theories should be modified if they do not provide convincing explanations so that they can then be used in future case studies. Similarly, Corbin and Strauss (2008) suggest that an existing framework could be used to complement, extend, and verify the findings of the study and offer alternative explanations to the findings as well as assist the researcher in developing a middle-range theory (p.39).
The use of theories in accounting research is important because in order to generate findings that are of interest to the wider accounting research community, the qualitative field researcher must be able to continuously make linkages between theory and findings from the field in order to evaluate the potential interest of the research as it unfolds (Ahrens & Chapman, 2006, p.837). However, accounting researchers are cautioned to apply prior theories in a less constrained way so that the framework is open to being challenged and refined. This would enable the development of a theoretical framework that focuses explicitly on the issues and questions raised by the case (Humphrey & Scapens, 1996). Furthermore, the researchers are advised to avoid forcing theoretical constructs onto the data, but instead allow the constructs to emerge from the data (Ahrens & Dent, 1998). Vaivio (2008) warns that if the researchers strictly adheres to pre-specified constructs, he or she could end up forcing these preordained perspectives onto the observations and thereby suffocating any potential empirical insights (p. 74).

The theory being proposed in this research will be used primarily to framing the research question, and to guide the reflection on and interpretation of themes arising from data analysis in order to develop new and deeper understanding of the events observed during the research. Although the proposed theory is being used in this research, the analysis shall not be restricted only to observations explainable by this theory but will remain open to possible alternative explanations to issues uncovered. In doing so, the research could possibly discover new relationships, new orientations, or new phenomena that current theory and theoretical perspectives have not captured (Dyer & Wilkins, 1991). Therefore, the use of this framework is representative of the approach ‘middle-range thinking’ (Laughlin, 1995, p.77), where the framework is used as a means to guide reflection on empirical reality but not constraint the understanding of the situation.
4.2 Theoretical Approaches to Disclosure

The study of financial disclosure has been approached from a number of theoretical perspectives, namely, agency theory, stakeholder theory, institutional theory and grounded theory. Each of these theories is discussed below.

4.2.1 Agency theory

Agency theory, a seminal work of Jensen and Meckling (1976), is based on the conflict of interests existing between the shareholders who act as the principals and the managers of the companies who act as agents, in situations where there is a separation between the ownership and management or in the separation of risk bearing, decision making and management functions (Jensen & Meckling, 1976; Fama & Jensen, 1983). Jensen and Meckling (1976, p. 308) define the agency relationship as “a contract under which one or more (principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision-making authority to the agent”. In general, it is presumed that the agent has more information of the organization activities than the principal. Unfortunately, the agent is driven by self-interest and undertakes self-serving activities that could be detrimental to the economic welfare of the principals (Jensen & Meckling, 1976). Therefore, agency costs arise in order to monitor agents’ behavior and bonding agents’ interests with the principals’ interests. Agency theory suggests that disclosure enables principals to monitor managers’ behavior while reducing agency costs (Khlifi & Bouri, 2010).

Healy and Palepu (2001) employed agency theory in disclosure by analyzing information asymmetry between the managers acting as agents who disseminate the information and the users of that information (investors and other stakeholders). They argued that disclosure only serves to reduce this asymmetry as it seems that information asymmetry will always exist due to the conflict of interests between the agent and principal – the maximization of their individual interests. Similarly, disclosure is suggested to be able to reduce information asymmetry between informed and badly informed investors, and consequently increases liquidity on the market (Kim &
Verrecchia, 1994). Some of the studies have sought to explain differences in disclosure among firms with different audit quality, leverage, firm size, and industry classification which have been identified as significant explanatory factors for disclosure (e.g. Morris, 1987; Hossain et al., 1995; Watson, Shrives & Marston, 2002; Archambault & Archambault, 2003; Xiao, Yang & Chow, 2004; Leventis & Weetman, 2004). To sum up, disclosure provides managers with the opportunity to increase their transparency to capital markets, reducing information risk and cost of capital and increased share price and liquidity (Beattie & Smith, 2012).

Agency theory has however, been subjected to several limitations. Firstly, the theory excessively focusing on the principal–agent relationship (particularly the shareholder-management relationship) and ignores the agent’s relationships with other-related individuals or groups (e.g. suppliers, customers, government and other local authorities) which also affect the operation of an organization. Secondly, agency theory is inappropriate for the public sector due to the multiplicity of principals and agents. There are no owners who have a material interest in the organization (Frumkin & Galaskiewicz, 2004). Thirdly, the theory puts emphasis on monetary terms to measure the performance of agents whereas in public sector, output and performance are often more difficult to measure given the nature of the goods and services produced (Frumkin & Galaskiewicz, 2004). Fourthly, agency theory is silent on the various forces which shape disclosure behavior such as the institutional environment. Majority of disclosure studies using agency theory have focused on corporate characteristics, which are in fact the reported results rather that the process that products the reports. As such, these studies have largely ignored the social and environmental factors (Hopwood, 2000) that have an impact on disclosure behavior. Finally, it does not enable an analysis of internal decisions and actions regarding disclosure.

4.2.2 Stakeholder theory

Stakeholder theory is concerned with the relationships of an organization with a variety of stakeholders in society where these stakeholders have an interest in actions and decisions of the organization. Stakeholders have been defined by Freeman (1984) as “groups and individuals who can affect or are affected by the achievement of the
organization’s objectives such as shareholders, employees, customers, suppliers, distributors, competitors and society in general” (p.46). There are two branches in stakeholder theory: the managerial branch and the ethical (moral) one (Beattie & Smith, 2012). The managerial branch of stakeholder theory attempts to explain and predict how the organization deals with demands of various stakeholders. Since various stakeholders have different needs and wants, there have been some attempts to distinguish and classify stakeholder groups (e.g. Clarkson, 1995; Mitchell, Agle & Wood, 1997) with a focus on identifying those considered to be most critical or powerful to the organization’s ongoing survival (Beattie & Smith, 2012). Bailey, Harte and Sugden (2000) suggest that organization respond to those stakeholders that are deemed to be powerful. Similarly, Neu, Warsame and Pedwell (1998) found that companies were more responsive to the demands (or concerns) of financial stakeholders (shareholders, creditors and government regulators) than the concerns of environmentalists because they possess power over a firm’s financial resources. The managerial stakeholder branch advocates that the greater the power of particular stakeholders, the greater the expectations of the stakeholders will be addressed by the management of the organization (Guthrie, Petty & Ricceri 2006). The ethical (moral) branch of stakeholder theory purports that different stakeholders have a right to information and that right should be protected by the organization.

From the stakeholder theory perspective, an organization’s continued existence requires the support of the stakeholders so they should be managed if the organization is to survive and be successful in the long run (Deegan, 2006; Gray, Kouhy & Lavers, 1995). Information disclosure is seen as a major element that can be used by organizations to manage or to manipulate the stakeholder, in order to gain their support and approval, or to distract their opposition and disapproval (Gray, Owen & Adams, 1996). Thus, stakeholders can potentially drive voluntary disclosure (Beattie & Smith, 2012). In this perspective, the information disclosure is considered to be ‘responsibility-driven’ (Beattie & Smith, 2012, p.4). Stakeholder theory also has limitations in explaining and predicting organizations’ disclosure practices. Firstly, it does not prescribe what information and how much information an organization should disclose. More specifically, this theory does not attend to how the decisions regarding disclosure are made within an organization. Secondly, in the public sector, there are many
stakeholders and identifying them is not easy. Moreover, there is no actor who has a direct financial interest in the organization, and thus no actor has a material stake in monitoring its operation and performance (Frumkin & Galaskiewicz, 2004).

4.2.3 Legitimacy Theory

Legitimacy theory is based on the notion of a social contract that exists between the society and an organization. Thus, it purports that organizations should continually seek to ensure they operate within the bounds and norms of respective societies (Deegan, 2006). Suchman (1995, p.574) defined legitimacy as:

A generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definition.

The theory emphasizes the recognition of society at large whereby failure to comply with the societal expectations may result in sanctions being imposed in the form of restrictions on operations, resources and demands for its products (Deegan, 2006). Dowling and Pfeffer (1975, p. 122) claim that “organizations will take various actions to ensure that their operations are perceived to be legitimate”. To appear legitimate, a firm needs to identify community expectations and important stakeholders and manage the potential legitimacy gap (Chalmers & Godfrey, 2004). According to Suchman (1995), legitimacy-threatening issues can be created by the media, regulatory or institutional pressures, evolving social awareness and/or corporate/industry crises. Information disclosure are argued as one of an effective means or strategies to be utilized by an organization to gain, maintain and repair legitimacy as well as to legitimate its existence (Dowling & Pfeffer, 1975; Lindblom, 1994; Branco & Rodrigues, 2007; Beattie & Smith, 2012). Some studies provide support for this argument (see for example, Deegan, 2002; O’Donovan, 2002 and O’Dwyer, 2003). In short, legitimacy theory comprises of two factors (Dowling & Pfeffer, 1975). Firstly, the activities developed by the organizations must be in accordance with social values of the society in which it operates. Secondly, those activities must be communicated to the society through the disclosure made by the organization. This communication is
however strategic with the aim of either retaining or winning stakeholder support with disclosure viewed as a mechanism for achieving these aims.

4.2.4 Institutional Theory

Legitimacy theory and institutional theory have similarities and are sometimes treated as being the same thing. There are however, some differences. The common thread between these two theories is how to obtain legitimacy, but institutional theory looks at the forces and the pathways through which organisations attain legitimacy while legitimacy theory emphasizes ways in which organizations can be legitimate to various stakeholders and how legitimacy can be managed to satisfy or even win them. The central issue in institutional theory is that an organization’s survival requires it to conform to social norms of acceptable behaviours in order to gain legitimacy (Meyer & Rowan, 1977; DiMaggio & Powell, 1983; Scott 1987; Brignall & Modell, 2000). Institutional theory assumes that formal organization structure, policies and procedures are shaped by their social environments. DiMaggio and Powell (1983) and Scott (2003) argue that institutional theory adopts an open system perspective whereby the organizations are influenced by their environments on both how they are structured and how they carry their work. These influences are not only by competitive forces and the need for efficiency, but also by socially constructed beliefs and rule systems. Covaleski and Dirsmith (1988) argue that “many aspects of an organization’s formal structure, policies and procedures serve to demonstrate conformity with institutionalized rules, thereby legitimizing it, to assist in gaining society’s continued support” (p.563). With regard to the public sector, Carpenter and Feroz (2001) state that “institutional theory suggest that an organization’s tendency toward conformity with predominant norms, traditions and social influences in their internal and external environments will lead to homogeneity among organizations in their structures and practices, and that successful governments are those that gain support and legitimacy by conforming to social pressures”(p.569). Therefore, they suggest that in order to gain legitimacy, government organizations will eventually tend to adopt similar financial reporting practices. In some instances, the organizations may adopt certain characteristics in order to appear legitimate, even though sometimes there are no technical economic efficiency gains
from doing so (DiMaggio & Powell, 1983; Hyndman & Connolly, 2011). In line with this, organizations, as Meyer and Rowan (1977) suggest tend to be homogeneous in their practice through a process of isomorphism to reflect institutionalized rules. In relation to financial disclosure, the organizations may disclose financial information to demonstrate their compliance with the social values reflected in regulations and informal norms (Gibbins et. al., 1992).

Due to environment pressures, the commitment of an organization towards ‘good’ disclosure practice and management could be a result of isomorphism. Hannan and Freeman in DiMaggio and Powell (1983) argued that “isomorphism can result because nonoptimal forms are selected out of a population of organizations or because organizational decision-makers learn appropriate responses and adjust their behavior accordingly” (p.149). DiMaggio and Powell (1983) identify three mechanisms that pressures organization to adopt institutional practices: coercive isomorphism, mimetic isomorphism, and normative isomorphism. Coercive isomorphism, according to DiMaggio and Powell (1983) “results from both formal and informal pressures exerted on organizations by other organizations upon which they are dependent and by cultural expectations in the society within which organizations function” (p.150). Some studies have employed institutional theory in order to explain the accounting choice in public sector (e.g. Carpenter & Feroz, 1992, 2001; Frumkin & Galaskiewicz, 2004; Ryan & Purcell, 2004; Baker & Rennie, 2006; Pilcher, 2011). For example, Carpenter and Feroz (1992) draw on institutional theory to explain the state of New York’s decision to adopt GAAP. In conclusion, they suggest that the state’s decision to adopt GAAP was an attempt to regain legitimacy for the state’s financial management practices. Similarly, Pilcher (2011) suggest that in order to maintain of legitimacy, local councils have complied to varying degrees with IFRS.

Institutional theory has however, been subjected to criticism for excessively emphasizing the external environment. The theory does not provide knowledge on how disclosure decisions are made within the organization. The theory assumes there is no internal agency i.e. people are robots. Moreover, the theory is not concerned with whether the legitimizing strategies do work, and if so, which forms of disclosure
medium (e.g. annual reports, newspapers, or electronic media) are more useful for the organization to implement the strategies.

4.3 Choice of Theory: Grounded Theory - The Gibbins, Richardson and Waterhouse Model (1990)

Due to the limitations to the theories discussed above, the model of Gibbins et al. (1990) has been chosen for this study. The Gibbins et al. (1990) model is an empirically derived structure designed to explain and predict an organization’s or firm’s financial disclosure. Just like other functions in the organization, this model views financial disclosure as a managed activity. According to Gibbins et al. (1990) the way in which financial disclosure is managed can have significant consequences for the organization. If we understand why and how financial disclosure is managed, we should be able to make better predictions of the outcomes. The motivations, events and processes, structures and people behind financial disclosure, if understood, would give us a better perspective of the outcome. Thus, this should enable us to improve our understanding of disclosure.

Gibbins et al. (1990) defined financial disclosure as “any deliberate release of financial information, whether numerical or qualitative, required or voluntary, or via formal or informal channels” (p.122). This model was developed by Gibbins et al. who applied a grounded theory methodology. In their field-based study of disclosure practices, the authors analysed the transcripts of 20 interviewed people involved in the disclosure process of Canadian companies, from which they developed a model to explain organization financial disclosure. The authors argue that “the use of a grounded theory method helps to ensure that the variables and relations developed describe the experiences of those who make disclosure decisions” (p.122).

The Gibbins et al. model is considered an ideal framework to inform this study. There are several reasons for the choice of the Gibbins et al. model to investigate the disclosure practices in MLAs. Firstly, this model embraces both organizational and environmental influences on disclosure strategy (Adams, 1997). Thus, it overcomes the limitations of institutional theory for excessively emphasizing the external environment.

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5 The model was later expanded by authors in Gibbins, Richardson and Waterhouse (1992).
and agency theory for ignoring institutional factors. Organizational and environmental influences, particularly institutional influences provide a good insight into financial disclosure practices in the public sector due to its nature. As such, this model is more appropriate to be applied to the public sector as compared to agency theory and stakeholder theory. These two theories put more emphasis on an open market environment, and thus are more appropriate to be used to study disclosure practices in private sector environment. With regards to institutional influences, Gibbins et al. (1992) argue that the organization’s survival depends on the ability to comply with the rules set by powerful actors and thus to maintain access to the resources controlled by those actors. The organization is, therefore, coerced by its influential or powerful stakeholders into adopting particular voluntary disclosure practices. This view is consistent with institutional theory’s coercive isomorphism.

Gibbins et al. (1992) argue that “in spite of these uncertainties, organizations which disclose financial information must achieve closure and settle on particular accounting policies, presentation formats, and distribution systems. These choices are often made on the basis of informal ‘rules’ shared within particular communities” (p.51). This view is akin to normative isomorphism in institutional theory and stems from professionalization that describes the effect of professional standards and the influence of professional communities on organizational characteristics. Normative isomorphism is related to the ways in which organizations are expected to conform to standards of professionalism and to adopt systems and techniques considered to be legitimate by relevant professional groupings (Ashworth, Boyne & Delbridge, 2009). According to Gibbins et al. (1992), the ability of professionals to exercise normative influence within organizations is enhanced by three features. First, many professionals see their peers in other organizations as their reference group and this apparently provides them with a standard behaviour which allows them to resist pressures to react to local conditions. Second, the flow of professional personnel between regulators and regulated firms provides members with tacit knowledge of regulatory process and creates expectation that professionals will be able to identify and anticipate the actions of regulators. Finally, accounting standards are written to explicitly allow accountants to use their judgement in reporting economic events.
Secondly, this model is specifically designed to explain and predict an organization’s or firm’s financial disclosure and thus address the limitations of stakeholder theory, which is more concerned with the relationships of an organization with a variety of stakeholders in society. Thirdly, the model is based on an extensive review of the disclosure practices and management literature. Therefore, many factors associated with disclosure as addressed by agency theory, stakeholder theory and institutional theory have been considered. Fourthly, the model describes the managers’ discretionary behaviour in a more comprehensive manner than most other analytical and empirical models do (Trabelsi, Labelle & Laurin, 2004).

Fifthly, the model examined both the quantitative and qualitative aspects of published annual reports in order to explain corporate financial disclosure. Finally, the model has already been used in a number of firms’ financial disclosure studies (e.g. Aerts, 2005; Holland, 2005; Trabelsi, Labelle & Laurin, 2004; Botosan & Harris, 2000; Adams, 1997; Holland & Stoner, 1996; Waterhouse, Gibbins & Richardson, 1993).

The choice of this model is also informed by the authors’ awareness that this model has never been used to explain the financial disclosure management and practice in the public sector. As discussed earlier this model embraces both organizational and environmental influences on disclosure strategy. Organizational and environmental (particularly institutional influences) influences can help in the study of financial disclosure practices in local government. Therefore, this model may provide fruitful insights into explaining the financial disclosure practice and disclosure management in the public sector in MLAs. More specifically, this model is applied in order to provide guidelines to delineate those who could make disclosure decisions in the organization, the range of issues considered when making disclosure decisions, the role of external parties (e.g. auditor) in the disclosure decision, and the impact of external disclosure rules on disclosure decisions.

4.4 Description of Gibbins et al. (1990) Model

Gibbins et al., (1990) argue that “the disclosure process involves producing output in response to internal or external stimuli” (p.128). The organization’s readiness to disclose is a function of its developed disclosure position, the existence of internal or
external structures for handling disclosures, and the presence external mediators such as auditors and consultants. Disclosure position according to this model has a number of significant internal and external antecedents and these antecedents may affect structure and the use of external mediators and the disclosure position itself. Gibbins et al. (1990) further explain that any disclosure norms and opportunities are or maybe identified as management perceive an issue having disclosure implications. The identification of issues and the perception of associated norms and opportunities may be influenced by disclosure position, mediators and structure. A function of the perceived norms and opportunities, the disclosure position’s ritualistic and opportunistic dimensions, and any existing structures subsequently produced disclosure outputs.

Gibbins et al. (1990) argue that external and internal antecedents strongly influence whether and how disclosure issues are perceived. They further argue that organizations are predisposed to ritualistic and opportunistic behaviour in the management of disclosure as a result of firms’ history, attitude of the management and the degree of internal consensus on disclosure issues as well as a consensus or as a compromise from internal politics on disclosure issues. Gibbins et al. (1992) contend that the degree to which sub-unit or individual managers in the organization are given discretion over disclosure decisions will determine the nature of the entity’s disclosure strategy. They add that their conceptual framework of corporate disclosure “...adopts an “open system” view of organization structure and processes wherein organizations are seen as capable of adopting to changes in their environment...” (p.60). The framework therefore holds that the operating environment influences organizational conditions and the perceptions, and subsequently influences the disclosure decisions.

The Gibbins et al. (1990; 1992) also discusses the two environmental attributes - economic factors and institutional influences that are most relevant to organizational condition under their framework. They argue that “...the firm’s economic context ......its positioning in factor and product markets, present the firm with disclosure opportunities...” (p.73). Whether these opportunities will be perceived depends on the firm’s disclosure position and on the strength of the economic stimuli.

The Gibbins et al. model incorporated institutional influence where the presence of strong institutional environments give rise to rules that enable efficient exchanges and
legitimate particular behaviours and is likely to be positively associated with a ritualistic dimension to the firm’s disclosure position and perception of issues. Gibbins et al. (1992) argue that the institutional perspective mainly focuses on the environment in which the financial disclosure occurs. It views the disclosing organizations as being embedded in a web of social relations which structure the way in which financial disclosure may be managed. Their concern is more on the impact of institutional influences on the internal management processes leading to financial disclosure. To cite Gibbins et al. (1992), “this approach tends to regards institutions as exogenous to the financial disclosure process and allows for possibility that the institutions which affect financial disclosure evolve due to social forces other than the search for economic efficiency” (p. 42). The survival and continued existence of organizations require them to maintain the legitimacy. In this respect, they viewed the institution as a set of rules that constrains and enables human interaction. (p.41) and the financial disclosure is a “communicative process embedded in a web of social relationships” (p.57). Therefore financial disclosure is designed to comply with rules and to reflect informal norms (p.57). Based on the Gibbins et al. explanation a similar concept of institution and financial disclosure are therefore adopted in this study.

Although Gibbins et al. (1990) considered both economic factors and institutional influences in their model; the institutional influences dominate this study due to the nature of local government. The arguments for this were presented by Frumkin and Galaskiewicz (2004), who first argued that the public sector is susceptible to institutional factors because outputs are very difficult to evaluate. In other words, public organizations would be vulnerable to institutional influences due to lack of accountability for financial indicators (such as sales and profits) as their outputs are often difficult to measure. Additionally, they argue that the public organization operates under a ‘nondistribution constraint‘. There is no distribution of public sector earnings due to no people having a direct financial interest in the organization, and thus no person has a material stake in monitoring its operation. Frumkin and Galaskiewicz (2004) argue that the performance of government organizations is less accurately measured and monitoring is more infrequent as compared with business organizations whose purpose is to earn profits and monitoring is more frequent. Government organizations according to them are more likely to embrace external referents of accountability to legitimate their operations due to lack of a single stakeholder group to
monitor the organization and rigorous criteria for evaluation. Therefore, government organizations should be more susceptible to institutional pressures and more likely to be influenced by exposure to environmental pressures that promise an organization greater legitimacy.

Secondly, Frumkin and Galaskiewicz (2004) argue that the public sector organizations are susceptible to institutional factors because of their structure tend to be more bureaucratized. They argue that the flow of financial inputs in government is harder for stakeholders to change and demands a much higher level of coordination and collective action. Therefore, the sources of government funding that is taxpayers, exercise less direct control over government organizations, which creates accountability problems. They further argue that “this is often one rationale that public administration theory offers for why public sector organizations are more bureaucratized” (p.291). Further, this argument is related to the role of the government organization as funding provider and regulator of business activities. The multiple roles of government organizations in the implementation of certain policies and procedures require compliance by lower level of governments. Frumkin and Galaskiewicz (2004) argue that “external supervision by government oversight institutions and authorities may also affect the ability of lower levels of government to carry out significant changes in policy and procedure….the ability of government to maintain a fair measure of control over the flow of inputs is a function of its ability not just to collect taxes and assess fees but also to win public approval so that decisions about the allocation of resources end up favoring one purpose or agency over another” (p.291).

This view is consistent with Carpenter and Feroz (2001), who suggest that institutional factors provide better insights into understanding accounting practices in the public sector. They argue that economic variables may no longer continue to be significant variables in explaining the accounting rule choice in the public sector because it regularly has ambiguous goals and unreliable performance measures. Consequently, given the above explanation, the institutional factors/influences are expected to come to the fore in this study. As MLAs constitute one form of government in the public sector, their accounting and disclosure practices are also subject to institutional factors. The Gibbins et al. (1990) model is figuratively depicted in Figure 4.1.
4.4.1 Disclosure Outputs

Disclosure outputs are the components that the organization attempts to manage. With regards to this, Gibbins et al. (1992) argue that:

financial disclosure as being to some degree managed, as other activities of the organization are managed, and so involving a variety of actions in connection with various problems and goals…the result of disclosure management is not just a single number, such as earnings per share, or a set of reports, such as the annual financial statements. Rather, the result is a broad, multidimensional
array of numbers and words, released at various times of the year in various media and connecting in various ways with other disclosures (p.15).

They categorized managed disclosures into eight categories. The first category is data content which they refers to the quantitative and qualitative data disclosed. This is raw data around which other disclosure dimensions exist and is the feature of financial disclosure that is most studied by accounting researchers (Gibbins et al., 1992). Gibbins et al. (1990, 1992) identify other categories of disclosure output, these being data organization, prior or concurrent interpretation by the discloser, medium, timing, redundancy, credibility and subsequent interpretation by the discloser. Data organization is the arrangement of the information for presentation. Prior or concurrent interpretation by the discloser is any attempt to manage the interpretations that are to be given to the data. The aim is to influence the way the user understands financial information released by the firm. The medium is a variety of media or channel through which financial information is released. Gibbins et al.’s model distinguishes official written documentation such as annual reports or securities filings from other channels, such as news releases, electronic data transfers, speeches and phone calls. The Gibbins et al. model distinguishes between the medium and the content “because of anecdotal evidence and suggestions from disclosure inventories…that the content is often released through several media” (1992, p.19). The medium may be chosen because it is thought to carry implications of its own (Gibbins et al., 1992: p.19).

The time dimension involves management of two components, date and frequency of financial disclosure. Redundancy in disclosure occurs when the same data are released in more than one way or at more than one time. The credibility of the data in the disclosure may be managed by involving third-party enhancers such as auditors, legal counsel or other perceived people as well as through slogans and pictures of corporate activities. Subsequent interpretation by the discloser arises because the release of financial information triggers third-party interpretations which motivate management to “correct” the meaning apparently being given to the data (Gibbins et al., 1992). There may be attempts to correct news stories or suggest to analysts that forecasts are inaccurate.
In this study, the disclosure output component is used to identify the mediums of disclosure, the frequency of the disclosure, and the determination of the data content and data organization of MLAs.

4.4.2 Disclosure Position

Disclosure position is a variable empirically identified and defined by Gibbins et al. (1990, p.130) as “a relatively stable preference for the way disclosure is managed”. Disclosure position determines the firm’s expected or usual response to disclosure issues under normal circumstances. In other words, it is a way of representing the shared meanings and understandings among the firm’s managers of the appropriate behavioural responses to issues (Gibbins et al., 1992). The Gibbins et al. (1990) model identified two key dimensions of managers’ disclosure position – ritualism and opportunism. Gibbins et al. (1990, p. 130) defined ritualism “as a propensity toward uncritical adherence to prescribed norms for the measurement and disclosure of financial information”. The ritualistic dimension implies a passive adherence to perceived disclosure norms by using routinized, bureaucratized procedures. Ritualistic behaviour is repetitive and the role of managers in the disclosure is passive. The second dimension – opportunism – refers to a manager’s “propensity to seek firm-specific advantage in the disclosure or nondisclosure of financial information” (Gibbins et al., 1990, p. 130). It involves an active role for managers in which disclosure is an opportunity to obtain specific advantages by managing the disclosure process. Therefore, Gibbins et al. (1992) argue that both ritualism and opportunism are the key variables in explaining how financial disclosure is managed.

In this study, this component is used to identify the disclosure position of the person/committee responsible for disclosure decisions on disclosure antecedents or issues.
4.4.3 Disclosure Issues, Norms, and Opportunities

Gibbins et al. (1992) argue that the disclosure processes and output are activated by the perception of disclosure issues, according to the norms and opportunities perceived in each. The norms and opportunities perceived to apply to the situations are identified and put to work. Disclosure norms may be partially external disclosure requirement and regulations or partially internal rules established by the firm. Opportunities on the other hand are perceptual and are the benefits and costs that the managers believe to be associated with specific disclosure issues. An opportunistic position is more likely to be adopted where many issues with opportunities are present. In contrast, a ritualism disclosure position is activated by the perceived presence of external norms. Repeated exposure to issues with strong norms may increase the propensity to ritualistic behaviour (Gibbins et al., 1990).

4.4.4 Antecedents

The Gibbins et al. model theorized that a firm’s specific disclosure position is understandable in terms of series of internal antecedents and external antecedents. Internally, the disclosure position of the firm may be influenced by the firm’s history – that is, the firm’s traditions, taken-for-granted ways of doing things and its experience and expertise in financial disclosure. Furthermore, the firm’s disclosure position may also be shaped by its corporate strategy – that is the attitude of the CEO and the degree of internal consensus on disclosure issues. The disclosure position may also emerge either as a consensus or as a compromise from internal politics on disclosure issues. On this theme, disclosure position is also determined by the firm’s external economic and institutional environments. The firm’s position in the market factor such as the frequency of using financial market and the firm’s competitive position in product markets influence the extent of financial disclosure. Institutional factors, including legislation regulations and standards, and the existence of interorganizational networks and industry norms also affect the firm’s disclosure activities through their effects on disclosure position.
Consistent with this, Carpenter and Feroz (2001) state that the pressures created by institutional and organizational factors on accounting choice in the public sector are generally ignored in previous studies on governmental accounting. They argue that non-economic factors such as organizational values, politics and institutional norms may determine bureaucratic self-interest and these factors are important in explaining accounting choice in the public sector.

In this study, this component is used to identify the range of issues considered when making disclosure decisions.

4.4.5 Structures

The importance of the firm’s institutional and market factors shape the internal and external structures of the firm, which act as activating forces for the disclosure process. Gibbins et al. (1990, p.133) argue that “there will be more disclosure activity for a given disclosure position if structures are in place”. They defined internal structure as “the extent to which responsibility for the management of the disclosure process is assigned to particular positions within the organization and/or it is guided by clearly understood policies and procedures” (p.133). Well-defined internal structures may exist for both ritualistic and opportunistic disclosure positions. External structure is defined by Gibbins et al. (1990, p.133) as “the extent to which external demands for information are channelled through organizations that claim to represent third-party interests”. To cite Gibbins et al. (1990) further “a highly elaborated set of external processes and procedures has an important impact on internal disclosure activities” (1990, p.133). For example, some recipients of information receive favourable treatment because of their role in external scrutiny that leads external structure to confidential disclosure.

In this study, this component is used to provide guidelines to identify those who could make disclosure decisions in the organization.
4.4.6 External Mediators

Firm managers may receive assistance from external consultants and advisors in identifying disclosure issues and related norms and opportunities. Gibbins et al. (1990) range potential advisors from those who have an institutional reason for being nearby such as external auditors, underwriters and corporate counsel to those consulted on an ad hoc basis. According to Gibbins et al. (1990), involving external consultants and advisors in the disclosure process may help identify issues, the specific formal or informal rules associated with a particular disclosure, provide technical advice and opinions which effectively shift some of the risk of decision-making away from management, and add credibility to disclosures. They may also be used as a strategic resource in bargaining situations where alternative interpretations of events are possible.

In this study, this component provides guidelines on the role of external parties (e.g. auditor) in the disclosure decision.

4.5 Chapter Summary

This chapter provides a theoretical framework for this study. Prior theories have the potential to provide deeper insights into accounting practices being investigated. This study employs the Gibbins et al. (1990) model, an empirically derived structure designed to explain and predict an organization’s or firm’s financial disclosure. The Gibbins et al. (1990) incorporate both organizational and environmental influences and identifies two environmental attributes - economic factors and institutional influences that are most relevant to organizational condition under their framework. Although this model considered both economic factors and institutional influences, the institutional influences are predominant in this study due to the nature of local government. The presence of strong institutional environments gives rise to rules that enable efficient exchanges and legitimate particular behaviours to occur, and is likely to be positively associated with the ritualistic dimension of the firm’s disclosure position and perception of issues.
CHAPTER FIVE
RESEARCH METHODOLOGY

5.0 Introduction

This chapter explains the research methodology adopted in this study. It is organized in the following manner. The next section presents the research methodology underpinning the study. This is followed by a discussion on research methods and the justifications for the use of the case study method. This chapter also describes the research design of the study, data collection procedures and the methods of data analysis. The validity and reliability features of the evidence are also discussed. The chapter ends with concluding remarks.

5.1 Methodology

Methodology is not only about the methods (Ahrens & Chapman, 2006; McGregor & Murnane, 2010) or the strategies of inquiry to be employed, but it is about the approach to the research (Ahrens & Chapman, 2006; Laughlin, 2004; Neuman, 2003). The scope of research methodology is wider than research methods. Research method basically refers to methods or technical procedures applied to conduct research (Kothari, 2004; McGregor & Murnane, 2010; Bryman, 2012). Kothari (2004) explain research methodology as follows:

when we talk of research methodology we not only talk of the research methods but also consider the logic behind the methods we use in the context of our research study and explain why we are using a particular method or technique and why we are not using others so that research results are capable of being evaluated either by the researcher himself or by others (p.8).

Basically, all research is based on some underlying assumptions. The differences between each research rest on ontological, epistemological, and methodological assumptions (Chua, 1986; Laughlin, 2004). The choice of research methodology therefore pivots on a researcher’s ontological assumptions, their fundamental beliefs about what is ‘real’ (ontology) and epistemology, which concerns the theory of knowledge, its nature and limits, and how people acquire and accept knowledge about the world (Bisman, 2010). As noted by Ryan, Scapens and Theobald (2002):
The assumptions which the researcher holds regarding the nature of the phenomenon’s reality (ontology), will affect the way in which knowledge can be gained about the phenomenon (epistemology), and this in turn affects the process through which research can be conducted (methodology). Consequently, the selection of an appropriate methodology cannot be done in isolation of a consideration of the ontological and epistemological assumptions which underpin the research in question (p.35).

At the two ends of ontological perspectives are realism, which view reality as subsumed with objects and independent of individual perceptions; and idealism, which view reality as subjective, socially constructed and existing in the mind of the subject (Ryan et al., 2002). The ontological assumptions have implications for the selection of research methodology because perceptions of reality relate to the way in which knowledge is understood. For example, when a researcher perceives the reality of an issue at question to be objective, knowledge about the issue is expected to be observable through empirical measurement (Kothari, 2004). This lends itself to quantitative research employing quantitative methods such as survey research, experimental research, non-reactive research (physical traces, archives and observation), and secondary analysis (content analysis) (Myers, 2009; Neuman, 2003; Goddard, 2010).

In contrast, where reality is perceived as subjective or ‘multiple’ (Creswell, 2007, p.17), knowledge about the issue is perceived as socially constructed requiring the researcher to ‘lessen the distance between himself/herself and the focus of research’ (p.17). This lends itself to qualitative research and often employs the qualitative methods of inquiry such as phenomenology, ethnographic studies, grounded theory research, case studies and narrative interrogation (Neuman, 2003; Creswell, 2007; Gephart & Richardson, 2008; Myers, 2009; Goddard, 2010).

Based on such previous works, a major premise of this study is that reality (about financial disclosure practices) is perceived as subjective and the knowledge about the issue is socially constructed phenomenon through human interactions (Burchell et al., 1980; Creswell, 2007). Therefore, this research was conducted using an interpretive case study, acknowledging the belief that social reality is not objective but highly subjective because it is shaped by individuals as they interact with each other (Collis & Hussey, 2009). Such a reality can only be better understood from the frames of
reference of those being studied (Creswell, 2007; Marshall & Rossman, 1995; Hopper & Powell, 1985). This research presupposes that the disclosure practices and management at the case organisations must be studied in its broader context. Further, the role of organizational and environmental factor in explaining financial disclosure must be considered. The researcher believes that the disclosure practices at the case organisations are complex, involving a number of actor, rules, values, norms, and interests. Thus, the disclosure at the case organisations is viewed as socially constructed by the interaction between the institution and its members, among individuals, and between the institution or individuals and their context, including their institutional, organizational, and social environments (Chua, 1986; Ahrens & Chapman, 2006). The interpretive approach is deemed appropriate for the study because the interpretive approach enables the researchers to capture the lived experiences of actors being studied (Chua, 1988) hence it leads researchers to seek a deeper understanding on the interaction and how the interaction constitutes the accounting practices. Baker and Bettner (1997) argue that “By examining accounting in the context of its metaphors, rituals, symbols and ceremonies, researchers have gained a more complete understanding of accounting’s capacity to reproduce values, norms, and ideologies, and mask conflicts in organizations and society” (p.306).

The interpretive approach also fits the aim of the research, which is to obtain a detailed understanding of the disclosure practice and management at the case organisations. This involves a consideration of values, beliefs, norms, and structures accepted by members of that institution, by which a qualitative method is said to be more advantageous in facilitating this compared to quantitative approach (Langfield-Smith, 1997; Neuman, 2003; Creswell, 2007; Gephart & Richardson, 2008; Myers, 2009; Goddard, 2010). The study was specifically guided by the Gibbins et al. (1990) model with the aim to understand and explain how financial disclosures are managed and practiced in MLAs. Further, the aim of this research is to explain how financial disclosure practices and management are influenced by various external and internal causes. To gain a deep understanding of the meaning of actions in a particular context, interviews were conducted with twenty-six people in 5 MLAs who were: heads of finance department/audit unit/evaluation department; assistant director/accountant/valuation officer; assistant accountant; assistant internal auditor; and public relations officer. Hence, consistent with interpretive approach, the researcher engaged with people in
their natural settings in order to understand the subjects’ perceptions of social reality (Parker, 2008). Therefore, the ontological and epistemological stance has given rise to research questions and a research methodology which call for an in-depth qualitative study (Creswell, 2007).

5.2 Research Methods

This study employed qualitative methods of data collection and analysis. Parker (2012) suggested that the application of qualitative research in accounting sets its sights on understanding how accounting processes and practices interact with, reflect and create specific organizational events, activities, and changes. Qualitative research has the advantage of developing depth, detail, rich and contextualized accounts of processes and practices. Qualitative inquiry often grounded in a philosophical position within the broad spectrum of interpretive sociology (Creswell, 2007; Broadbent & Unerman, 2011; Bryman, 2012), which is concerned to develop an understanding of aspects of social life that are not objectively given but are instead subjectively created through the interaction of actors (Ahrens and Chapman, 2006). Qualitative research focuses on issues of meaning and interpretation in the social world and often begins with assumptions, a worldview, the possible use of a theoretical lens, and the study of research problems inquiring into the meaning individuals or groups ascribe to a social or human problem (Creswell, 2007). It is also suggested that qualitative research has the capacity to build solid arguments about how things work in particular contexts or setting by talking directing with people and empowering individuals to share their stories, hear their voices, and minimize the power relationships that often exist between a researcher and the participant (Creswell, 2007). Bryman (2012) explained that qualitative research usually emphasizes words rather than quantification in the collection and analysis of data. The methods associated with qualitative research include the use of case studies, interviewing and document analysis. The following sections elaborate on these methods and how they are used in this study.
5.3 Case Study Methods

The case study has been defined by several scholars. For example, Yin (2009) defines the case study as “an empirical inquiry that investigates a contemporary phenomenon in depth and within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident” (p.18). To cite Yin (2009) further:

The case study inquiry copes with the technically distinctive situation in which there will be many more variables of interest than data points, and as one result relies on multiple sources of evidence, with data needing to converge in a triangulating fashion, and as another result benefits from prior development of theoretical propositions to guide data collection analysis (p.18).

Yin (2009) also states that case studies are suited typically to answer questions like “how” or “why”, noting that case studies are the preferred strategy when a researcher has little control over events and when the focus is on a contemporary phenomenon in a real-life context. Practitioners find “how” questions to be particularly important as they provide details in order to help convert private knowledge into publicly available knowledge (Cooper & Morgan, 2008). Case studies also illustrate why something was done or came to be, or when and why something works (Cooper & Morgan, 2008).

Eisenhardt (1989) defines case study as “a research strategy which focuses on understanding the dynamics present within single settings” (p.534). Eisenhardt (1989) further explains that case studies can be carried out in either single or multiple cases and can involve numerous levels of analysis. It is possible to conduct case studies at multiple levels of analysis within a single study. Moreover, the evidence collected can be qualitative, quantitative or a combination of both (Eisenhardt, 1989). In their definition, Cooper and Morgan (2008) see case study research as “an in-depth and contextually informed examination of specific organizations or events that explicitly address theory....” (p. 160). Cooper and Morgan (2008) further assert that case studies focus on bounded and particular organizations, events, or phenomena, and scrutinize the activities and experiences of those involved, as well as the context in which these activities and experiences occur. The case study research approach is useful where the researcher is investigating:
complex and dynamic phenomena where many variables...are involved, actual practices, including the details of significant activities that may be ordinary, unusual, or infrequent...and phenomena in which the context is crucial because the context affects the phenomena being studied (and where the phenomena may also interact with and influence its context) (Cooper & Morgan, 2008, p. 160).

The use of case studies in accounting research is a recent development. Just over 20 years ago, accounting researchers (Hopwood, 1983; Kaplan, 1984, 1986; Palepu, 1987; McKinnon, 1988; Scapens, 1990) called for more field-based research in accounting. This has since eventuated in several studies (e.g. Adams, 1997; Scapens, 2004; Lillis & Mundy, 2005; Merchant & Van der Stede, 2006) that have advocated more use of field-based research in accounting. Merchant and Van der Stede (2006) assert that the number of field research publications in accounting has grown dramatically over the last two decades. Despite several criticisms of the case study method, such as that it can only find out things with no prior ‘scientific’ research in generating ideas, or that it requires rigorous empirical testing to be empirically valid (Cooper & Morgan, 2008), Scapens (2004) asserts that case studies are nonetheless popular methods in accounting research. Scapens (2004) argues that one of the reasons for the growing use of the case study method in accounting is due to the failure of quantitative analyses to explain accounting practices. He argues that the use of sophisticated mathematical and statistical techniques has failed to test the predicted relationship and findings lack significant correlations. Consequently, McKinnon (1988) suggests that the rising use of field research methods including the case study is due to the increasing recognition by accounting researchers of the need to study accounting within its organizational and social contexts.

Zakiah, Ainun and Norsiah (2010) assert that the field research methods are concerned with the interactions between humans, objects and institutions in making sense of events, behaviours and outcomes. Similarly, in accounting, field-based researchers are interested in: people (e.g. accountants, managers, external users); the socially constructed object (e.g. the accounting reports or budgets); and institutions in which accounting takes place as well as the interactions between these elements (Zakiah, Ainun & Norsiah, 2010). Thus, the best way to study accounting in its natural context is through field research (Ahrens & Dent, 1998; Merchant & Van der Stede, 2006). Moreover, Merchant and Van der Stede (2006) contend that the distinctive characteristic
of the case study method is that it involves “the in-depth study of real-world phenomena through direct contact with the organizational participants” (p.118). Field research methods are desired because they provide a “rich” understanding of the relevant phenomenon (Merchant & Van der Stede, 2006; Ahrens & Dent, 1998) which are often lacking in other forms of research.

Field research is carried out to provide descriptions that explain what is happening (Eisenhardt, 1989). They also serve to teach us about innovative, cutting edge practices in successful firms (Kaplan, 1984), and contribute to an understanding of accounting as techniques (Cooper & Kaplan, 1987; Patell, 1987). Some studies such as Dent (1987), Knights and Collinson (1987), Preston (1986), Nor Aziah and Scapens (2007) investigate the links between accounting and management or organizational processes. Case study research methods are also effective for theory building and for testing and refining existing theories (Eisenhardt, 1989; Merchant & Van der Stede, 2006). Case studies normally combine data collection methods. Depending on the problems and research questions being addressed, case studies reported in the accounting literature encompasses a variety of methods such as analysis of archival materials, observation, interviews, participation and quantitative techniques (Eisenhardt, 1989; Patton, 2002; Cooper & Morgan, 2008).

The growth of field research publications however, is primarily confined to the management accounting area (Merchant & Van der Stede, 2006). Therefore, Merchant and Van der Stede (2006) further suggest that the field research methods should be utilised more by researchers in others accounting areas. Hence, this current study was carried out in order to answer this call and to provide some contributions to the financial disclosure literature as well as case studies literature. Using the Gibbins et al. (1990) model, the aim of this study is to understand and explain how financial disclosures are managed and practiced in MLAs and to explain how financial disclosure practices and management are influenced by various external and internal causes. More specifically, the study seeks to investigate who in the organization make financial disclosure decisions, the range of issues considered when making disclosure decisions (e.g. company culture, historical precedent and tradition, internal financial regulation, dominant personalities and professional groups), the role of auditors and other external parties in the disclosure process, and the impact of external disclosure rules on
disclosure decisions. To gain a deep understanding of the meaning of actions in a particular context, the case studies were conducted in five local governments comprise of one city council, three municipal councils and one district council. Therefore, case studies in this research serve to create an in-depth analysis of specific organizations with the purpose of obtaining a thorough understanding of accounting practice. The above discussion suggests that the case study approach adopted in this research would help to understand ‘how’ and ‘why’ financial disclosure is practiced and managed in particular ways in the organization under study.

5.3.1 Choice of Case Study

Scapens (1990, 2004) explained that case studies can be used in a variety of ways in accounting research, by classifying them into five types: descriptive case studies, illustrative case studies, experimental case studies, exploratory case studies and explanatory case studies. Descriptive case studies basically provide a description concerning the nature of contemporary accounting practices, techniques and procedures that are normally used. However, they are not able to explain the question of what constitutes ‘best’ practice and ‘successful’ companies (Scapens, 2004, p.259).

Illustrative case studies illustrate new and innovative practices created by particular companies. Such case studies depict what has been achieved in practice. Experimental case studies are used to examine the implementation difficulties and evaluate the potential benefits of the newly developed accounting procedures and techniques proposed by accounting researchers. Exploratory case studies are intended to explore the possible reasons for particular accounting practices. This type of case study represents preliminary investigations intended to generate ideas and hypotheses that can be used for rigorous empirical testing such as survey methods and other quantitative techniques at later stage. Exploratory case studies are the first step in the research and often involve only a small sample. Finally, explanatory case studies explain the reasons for accounting practice. This study is an explanatory case study method. Justifications for doing are described in more detail below.
The choice of research method and research design is very much determined by the research questions (Scapens, 2004; Siti Nabiha, 2010). Scapens (2004) contends that the first step in case study research is to clearly specify what needs to be asked. The research questions can be determined by reviewing the existing research literature. Based on Scapens’ (1990, 2004) classification this case study is explanatory in that it is intended to explain the reasons for accounting practices and to explain accounting based on the researcher’s interpretations of people’s social meanings and perceptions in a specific setting.

In order to understand the subjects’ own description of social reality, interactions between the researcher and the subject are required. A case study approach is appropriate to study the subjects’ world intensively and emphasise the meanings behind human actions. Scapens (2004) argues that the explanatory case study is normally used when the researcher is attempting to explain the reasons for observed accounting practices. In a similar vein, Ryan, Scapens and Theobald (2002) explain that the purpose of an explanatory case study is to explain the reasons for observed accounting practices. The main focus of the explanatory case study is on the specific case. Theory is used if it enables the researcher to provide good explanations for the observed accounting practices. Available theories should be modified if they do not provide convincing explanations. Scapens (1990, 2004) argues that the objective of explanatory case study is to generate theory that provides convincing explanations of a certain case study or scenario. In explanatory case studies, Scapens (2004) further argued that the selection of cases should not focus on generalising the findings to a larger population; rather it should reflect the needs of theory development. In other words an explanatory case study is not meant to produce statistical generalisations but to develop or to test and if necessary to extend theory as is intended in this thesis.
5.4 Research Design

Research design involves planning of the research study, dealing with aspects such the location of a study sample selection, data collection, and analysis. In other words, it is about organizing the research activity, including the method of collection of data, which could achieve the research aims (Smith, Thorpe & Lowe, 1991). Cooper and Morgan (2008) state that a good case research study should begin with a careful design that includes identifying the questions, unit of analysis and criteria for interpreting the findings. They further argue that the case researchers should be able to effectively arrange and coordinate their activities such as carefully negotiating appointments, arrangements, and access, etc. Yin (2009) notes that the research question should drive the choice of what case to study, who to see, what to observe, and what to discuss. In a similar vein, Scapens (2004) points out that the case study research “requires clear research questions, a thorough understanding of the existing literature, a well formulated research design with sound theoretical underpinnings…above all excellent language skills” (p. 258). The following sections elaborate the research design of this study.

5.4.1 Research Setting

Scapens (2004) argues that the cases should be selected to enable the researcher to focus on the questions being addressed in the research and he added that the characteristics of the cases to be studied are defined by the research questions and the theoretical framework. It is imperative that the researcher select the cases that display those characteristics. Scapens (2004) asserts that some researchers approach case studies from a positive methodological perspective and their concern is to select a representative case so that the findings may be generalised to a larger population. The case study approach, however, does not view the case as a sampling unit and the aim is not to generalise the findings to a wider context. The purpose instead is to develop and extend theory and as such, selecting representative cases is not the objective. Therefore, it is the theoretical rather than statistical generalisation is the main objective of the research (Scapens, 2004). In similar lines, Eisenhardt (1989) argues that the selection of cases is one of the important aspects of building theory from case studies.
In this thesis, the MLA has been chosen for the study. The case studies were conducted in five local governments. These local governments comprise of one city council, three municipal councils and one district council. For the case of city and municipal councils, all of them have great growth potential because of their well-developed financial systems and fast growing information technology sectors (Setapa, 2003). These local governments, especially the city and municipal types are accommodated by a large number of manufacturing, services and trading activities, which will continue to attract local and foreign investors. All of these local governments are situated in the state of Selangor. Selangor recorded the country’s highest Gross Domestic Product (GDP) growth of 10.8 per cent in 2010 (Malaysian Department of Statistics, 2010). Selangor continued its dominance in the manufacturing sector, construction sector and services sector with a share of 30.0 per cent, 36.8 per cent and 23.5 per cent respectively in 2010 (Malaysian Department of Statistics, 2010). All of these factors are offering growing opportunities and responsibilities to the local governments which may require them to have a clear and efficient financial plan (Setapa, 2003). Thus, these local governments are the appropriate samples for examining the issue of financial disclosure.

The list of local governments was obtained from the official website of the Ministry of Housing and Local Government. The effort was made to contact as many local authorities as possible prior to the council’s confirmation to participate. It is a fact that the research culture in Malaysia is still not well developed and the fact that there are many bureaucratic procedures which need to be complied with, especially in relation to conducting a study in government agencies. Participating local governments were approached via the mayors/presidents and their secretaries. The initial contact was done by telephone and e-mail in January 2010, discussing the general aim of the research project. Initially, 19 local governments were contacted but due to pressure of work and other commitments, only 5 agreed to participate. This was enough to provide a mix of local governments of different characteristics in terms of size and organizational forms.

An official letter were then sent to the mayors/presidents and the secretaries of these five local authorities by March 2010 to request approval to conduct interviews with the relevant personnel. A follow-up letter was sent providing further details and the core interview questions. Other communication methods were also used to secure participation such as e-mail and telephone calls. These follow-up efforts were deemed
necessary due to the fact that it took a while for these councils to approve the interviews. To overcome the potential delay, initial contact was done four months prior to the tentative interview date (see Appendix 5.1). The interview guide was e-mailed to all the participants after the confirmation was received from each council (see Appendix 5.2). Each participant had the general interview questions for at least one month before the interview. The field site interview guide was prepared in both the English and Malay languages.

5.4.2 Data Collection

This study collected both primary and secondary data.

5.4.2.1 Primary Data

In this study, semi-structured, face-to-face interviews constituted the primary method of data collection. Interviews constitute one of the major data collection methods for case study analyses (Laughlin, 2004; Smith, 2003). As suggested by Yin (2009), to answer the “how” and “why” questions for this study, data were collected by using semi-structured interviews. Snow and Thomas (1994) assert that “interviewing involves asking questions of those who have information about a phenomenon that the researcher has not been able to observe directly” (p. 461). Interviews enable researchers to appreciate the different meanings that people place on their experiences in organizations and make it possible to create a more in-depth examination what is being investigated (Adams, 1997). Furthermore, by studying the accounting practices in their organizational context, a fuller understanding of the behaviour of people may be obtained. The actual practices in the organization, that is, what organizational members do rather than what they are supposed to do can also be observed. Hence, the study focuses not only on the formal accounting practices but also on what is actually practiced. Scapens (2004) contends that the semi-structured interviews allow the researcher for a wide framework for questioning. This allows the researcher to discuss the similar issues with a number of different people. In addition, a semi-structured interview allows the researcher to explore the issues in-depth and to follow up the responses that are given (Scapens, 2004). The evidence from the interviews was
supported by documentary evidence, informal observations and informal conservations with people in the organizations.

Interview data were collected from twenty-six interviewees and more than 90 per cent of those involved in the study are from an accounting background or have a basic accounting knowledge. Interviews were conducted with twenty-six people in 5 MLAs who were: heads of finance department/audit unit/evaluation department; assistant director/accountant/valuation officer; assistant accountant; assistant internal auditor; and public relations officer. The researcher engaged with people in their natural settings in order to understand the subjects’ perceptions of social reality. The following section defines the case study research in more detail.

The details of each interviewee’s background and position are presented in Tables 5.1 and 5.2. The data collection took place over four months (May to August 2010) and focused on accounting disclosure practice issues and the internal and external contexts affecting such practices. As shown in Table 5.1 the interviewees worked at different levels, held different positions and were from a variety of backgrounds. The views of people with different work backgrounds and experiences enable the researcher to obtain broader and diverging perspectives on the same topic or issue. The longest period of service is twenty-three years while the shortest employment duration is two years. The actual selection of the interviewees was done on an ongoing basis during the data collection stage at the research site. Suggestions, mostly from the Heads of Finance/Treasury Department or their senior assistants, were solicited about who to interview.

These interview questions were guided by the theoretical framework as well as the literature review. The language used in the interviews was mainly Malay but in some cases, where appropriate, a mixture of both English and Malay was used. However, this was not expected to impact on the thesis significantly because the objective was to ensure that the message was conveyed and understood clearly. All interviewees were expected to explain their own views in considerable detail. Depending on who was interviewed and the issues being discussed, the length of the interview ranged from forty minutes to two hours. This allowed time for the discussion and probing into any further issues raised by the interviewees. Interviews were tape-recorded (with the
interviewee’s permission) and the field notes were taken by the researcher throughout the sessions.

Arrangements for the meeting and briefing session were organized with the respondents. A problem encountered was the fact that the interview appointments were subjected to several changes due to the interviewees’ other work-related commitments. However, to overcome serious appointment rescheduling, the interviewees were contacted by phone calls one or two weeks before the actual interview session.

In this study, as stipulated by the La Trobe University’s Human Ethics Committee, ethically responsible research practice was applied in line with the National Health and Medical Research Council’s ‘National Statement on Ethical Conduct in Research Involving Humans’ and with University guidelines on ‘Ethics Approval for Research with Human Subjects’. This project was also approved by the same committee (see Appendix 5.3). In keeping with those ethical guidelines, each interviewee was given the Participant Information Sheet which was prepared in both the English and Malay languages (Appendix 5.4 and Appendix 5.5). The purpose of this sheet is to provide the participants with a plain language statement that clearly explains the aims of the project and the nature of the participants’ involvement.

Information contained in the interview and consent letter (such as participant’s anonymity and confidentiality, contact information, provision and collection of research instruments) were explained to the participants in a briefing session lasting approximately 10 – 15 minutes. All the interviewees were required to sign the consent form which was prepared in both the English and Malay languages (Appendix 5.6 and Appendix 5.7). This form confirms the willingness of people to be interviewed. The interview procedures were provided and explained to them and the consent letter was obtained from each person. During the interview, participants were asked to talk freely about the questions based on their own experiences. It was only in the last few minutes of the interview session that specific questions were posed and only if a major financial disclosure issue had been omitted from the discussion.
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<th>Council</th>
<th>Position</th>
<th>Department /Division</th>
<th>Length of Service (years)</th>
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<tbody>
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<td>Head of Finance Department (Director)</td>
<td>Finance</td>
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<td>Senior Assistant Director (Accountant)</td>
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<td>Assistant Accountant</td>
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<td></td>
<td>Assistant Director</td>
<td>Valuation &amp; Property Management</td>
<td>8</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>26 interviewees</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
All interview responses which have been translated from Malay to English are indicated by quotes. Attached to each quote are the respondent’s details including: respondent’s workplace in abbreviation and interview number, all of which are presented in brackets after the quotes (see Figure 5.1). However, to ensure anonymity, all respondents’ names have been taken out.

![Figure 5.1 Information Shown in the Bracket after the Quotes](image)

The research did not just prioritize one specific group (e.g. accountants). Rather, perspectives from different types of personnel were obtained (e.g. Internal Auditor, Public Relations officer, Valuation Officer). Data triangulation was performed in which the information from one source was assessed by comparing it to other sources of evidence and interviewing other people on the same issues (Scapens, 2004). All evidence collected was recorded in an ordered and coherent manner for subsequent analysis. In addition, field notes were converted into more formal record once each interview completed.

### 5.4.2.2 Secondary Data

The evidence from the interviews was further supported by the review of documentary evidence such as published sources in public records (newspapers and information provided on MLA’s websites), annual reports, monthly management reports, legislative documents, financial reports and other documents. All secondary data were used to supplement the interviews. Data gathered from multiple sources enhanced the researcher’s understanding and explanation of financial accounting disclosure practices and management (Nor Aziah, 2010).
5.4.3 Data Analysis

According to Maxwell (2009), there are three strategies for qualitative data analysis, these being categorizing strategies, connecting strategies and memos and displays. The categorizing strategies involve coding and thematic analysis. Maxwell (2009) explains connecting strategies as an attempt to understand the data in context and using various methods to identify the relationships among the different element of the text (p.238). Connecting strategies means looking for relationships that connect statements and events within particular contexts into a coherent whole. Maxwell (2009) argues that the analysis strategies should be compatible with the questions being asked. Thus, both categorizing and connecting strategies should be applied in qualitative analysis as ignoring one of them may run the risk of missing important insights (Maxwell, 2009). Memos and displays are important analytical tools in qualitative analysis because they facilitate e thinking about relationships in data and makes ideas and analyses visible and retrievable (Maxwell, 2009). While memos are normally used to stimulate and capture ideas about data, displays which include matrices or tables, network or concept maps serve two purposes: data reduction and the presentation of data or analysis in a form that can be seen as a whole. Thus, qualitative data analysis basically involves understanding and making sense of large amounts of data by reducing the volume of raw information, followed by identifying significant patterns, and subsequently drawing meaning from data and finally building a logical chain of evidence (Patton, 2002).

It is a common practice to begin data analysis on completion of data collection. Interviews were transcribed verbatim either at the end of the day or as soon as possible, and the transcripts along with the field notes were scrutinized and key themes highlighted. Thereafter coding was carried out. In translating the data from Malay into English language, accuracy and minimizing possible interviewer’s bias and error was adhered to. This process took a considerable amount of time since the researcher had to carefully listen and understand the tape-recorded interviews a number of times to ensure completeness and accuracy. The quotes were highlighted for incorporation into the data interpretation stage. The transcriptions and translations were reviewed by a person to determine if the translations were correct. This individual was a PhD student in Accounting, Malay is her native language and she understands the financial disclosure literature. The QSR NVivo 8 software package was used for storing, organizing, coding
and querying unstructured data. Back-up files were prepared for each audio-recorded interview. All the interview transcripts were then stored in both hard and soft copies.

Before the categorizing process, all interview data were read several times to gain familiarity with the information. There were three steps in the data categorizing process. The categorizing begins with data classification based on existing conceptual framework, allowing for free code of observations that do not fit with the theory (Malina & Selto, 2001). As shown in Table 5.2 and Figure 5.2, all data generated from the interviews were systematically analyzed and classified according to the themes laid down in the Gibbins et al. model (1990). The main themes in this study are internal structure, disclosure output, stakeholders, reason for disclosure, internal and external antecedents and causes, and external mediator.

Secondly, after the main factors were defined and categorized, the interview transcripts were read several times to identify the important sub-themes. Thirdly, where possible, these sub-themes were classified and coded under the relevant main themes identified in the first step. For example, those responsible for the financial information disclosure as mentioned by the interviewees are coded under ‘internal structure that is responsible for the financial disclosure’ theme. Categorized under ‘disclosure outputs’ are data content and organization, medium, frequency and adequacy. To those whom the councils disclosed their financial information is coded under ‘stakeholders’ theme. Reasons for disclosing are coded under ‘reason of disclosure’ theme. Antecedents are categorized into ‘internal and external antecedents’. Finally, those external parties who help or advise the councils in the financial disclosure issues are included in the ‘external mediator’ theme. For the purpose of the findings report, the themes were assigned to each research question as shown in Table 5.2.
<table>
<thead>
<tr>
<th>Research Question</th>
<th>Themes</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. By whom and how decisions regarding disclosure are made?</td>
<td><strong>1. Internal Structure</strong></td>
</tr>
<tr>
<td></td>
<td>• Treasury Department,</td>
</tr>
<tr>
<td></td>
<td>• Mayor/President</td>
</tr>
<tr>
<td></td>
<td>• Finance &amp; Assessment Committee</td>
</tr>
<tr>
<td>2. How does the organization disclose financial information and why does the local council disclose financial information?</td>
<td><strong>1. Disclosure Outputs:</strong></td>
</tr>
<tr>
<td></td>
<td>• Data content &amp; Organization</td>
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<tr>
<td></td>
<td>• Medium</td>
</tr>
<tr>
<td></td>
<td>• Frequency</td>
</tr>
<tr>
<td></td>
<td>• Adequacy</td>
</tr>
<tr>
<td></td>
<td><strong>2. Stakeholders</strong></td>
</tr>
<tr>
<td></td>
<td>• Councillors</td>
</tr>
<tr>
<td></td>
<td>• Management</td>
</tr>
<tr>
<td></td>
<td>• State Authority</td>
</tr>
<tr>
<td></td>
<td>• Auditor</td>
</tr>
<tr>
<td></td>
<td>• Ministry of Housing and Local Government</td>
</tr>
<tr>
<td>3. What are the antecedents and how do they influence financial disclosure decisions?</td>
<td><strong>3. Reason of disclosure</strong></td>
</tr>
<tr>
<td></td>
<td>• Required by Legislation (Act 171)</td>
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<tr>
<td></td>
<td>• Monitoring and Decision-making purposes</td>
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<tr>
<td></td>
<td>• Auditing purposes</td>
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<td></td>
<td>• Financial assistance</td>
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<td></td>
<td>• Budget approval</td>
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<td></td>
<td>• Openness and Transparency</td>
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<td></td>
<td>• Sharing the information</td>
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<td></td>
<td>• Feedback from the public</td>
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<td></td>
<td>• Change public mentality</td>
</tr>
<tr>
<td></td>
<td>• Attract the higher level governments’ (Federal and State) attention</td>
</tr>
<tr>
<td>4. What mediator and how disclosure decision is influenced by external mediator?</td>
<td><strong>Antecedents</strong></td>
</tr>
<tr>
<td></td>
<td><strong>External:</strong></td>
</tr>
<tr>
<td></td>
<td>• Federal Treasury Instruction &amp; Circulars,</td>
</tr>
<tr>
<td></td>
<td>• Regulation - Local Government Act 1976 (Act 171)</td>
</tr>
<tr>
<td></td>
<td>•Disclosure Practices of other councils</td>
</tr>
<tr>
<td></td>
<td><strong>Internal:</strong></td>
</tr>
<tr>
<td></td>
<td>• Firm’s history</td>
</tr>
<tr>
<td></td>
<td>• Management views</td>
</tr>
<tr>
<td></td>
<td>• Number and experience of professionals</td>
</tr>
<tr>
<td></td>
<td>• Council’s culture</td>
</tr>
<tr>
<td></td>
<td>• Desire of the council to become more transparent</td>
</tr>
<tr>
<td></td>
<td><strong>External Mediators:</strong></td>
</tr>
<tr>
<td></td>
<td>• External Auditor/Auditor General (AG)</td>
</tr>
</tbody>
</table>
Although most of the themes were consistent with the Gibbins et al. (1990) model, other themes rose that were not consistent with the Gibbins et al. (1990) model and they
emerged from their frequent occurrence in the interview transcripts. For example, desire of the council to becoming more transparent was not in internal antecedent of the model. All the emerging issues were identified and listed during the categorizing process. The classification of themes was modified several times based on discussions with researchers and colleagues who had the knowledge in analyzing the interview data (Parent & Deephouse, 2007). Initially, 40 themes and sub-themes were classified from the interviews transcripts but this was reduced to 38 when 2 themes/sub-themes were merged with other similar ones. These discussions help to minimize the risk of errors and biases in the classification procedure.

5.4.3.1 Cross-Case Analysis

Yin (2009) argues that multiple-case studies allow for “replication logic”, by which theory is tested through replications of findings among cases in the study. Yin (2009) explains that “each case must be carefully selected so that it either (a) predict similar results (a literal replication) or (b) predicts contrasting results but for anticipatable reasons (a theoretical replication)” (p. 54). The purpose for these replication procedures is to develop a rich, theoretical framework (Yin, 2009). These procedures can be done in what Yin (2009) described as the pattern matching analytic technique. Pattern matching logic compares an empirical-based pattern with a predicted one and if the pattern coincides, the internal validity of the evidence is proven (Yin, 2009). This technique can be done either with a single case or multiple cases. This study conducted pattern matching technique to test the predicted pattern of specific variables that were determined (defined by the Gibbins et al. (1990) model) prior to data collection.

Along similar lines, Eisenhardt (1989) argues that the data analysis can be done within case data as well as in a cross-case search for patterns. Eisenhardt (1989) further argues that the key to a good cross-case comparison is looking at the data in many ways. In order to analyze the data from five cases here, the tactics for cross-case patterns suggested by Eisenhardt (1989) were adapted. The strategy involves the selection of themes and then looks for within-group similarities coupled with intergroup differences. The outcome of these comparisons can be new constructs that the researchers did not anticipate. Consequently tables have been created and used to compare the cases in order to find similarities and differences. For example, in order to identify the
person/committee responsible for financial disclosure decision, the researcher looked for within-group similarities coupled with intergroup differences and arrived at the mayor/president and the FAC as being responsible for this decision.

These tactics make sure that the researcher goes beyond initial impressions and is able to improve the accuracy and reliability of the theory. As noted by Eisenhardt (1989, p. 541):

The idea behind these cross-case searching tactics is to force investigators to go beyond initial impressions, especially through the use of structured and diverse lenses on the data. These tactics improve the likelihood of accurate and reliable theory, that is, a theory with a close fit with the data. Cross-case searching tactics enhance the probability that the investigators will capture the novel findings which may exist in the data.

5.4.4 Case Study Reports

Yin (2009) argues that a single set of ‘cross case’ conclusions can be drawn from multiple cases. Yin (2009) added that the case studies can be conducted and written with many different motives and these motives vary from the simple presentation of individual cases to the desire to arrive at broad generalizations based on case study evidence but without presenting any of the individual case studies separately.

Yin (2009) categories written forms of case studies into four types; namely the classic single-case study, the multiple-case version of the classic single case, a multiple-case or a single-case study but does not contain the traditional narrative and the multiple-case studies only respectively. This study falls under the forth category. Yin (2009) explains that the multiple-case studies type of reporting has “no separate chapters or sections devoted to individual cases, rather the entire report consist of the cross-case analysis, whether purely descriptive or also covering explanatory topics” (p. 172). Yin (2009) added that in such report, “each chapter or section would be devoted to a separate cross-case issue, and the information from the individual cases would be dispersed throughout each chapter or section” (p. 172). Based on these arguments, the findings of this study are reported in ‘cross-case’ conclusions that cover evidence from multiple cases. Each chapter of this study covers separate cross-case issue in the attempt to answer the
research questions. The evidence from the individual cases was dispersed throughout each chapter.

5.5 Validity and Reliability of Evidence

In conducting case studies researchers are concerned with the reliability and validity of their evidence. According to Yin (2009), a major challenge here is to ensure that the data collection and analysis meet four tests: construct validity, internal validity, external validity and reliability.

5.5.1 Construct Validity

Construct validity according to Yin (2009) involves “identifying correct operational measures for concepts being studied” (p. 40). Here, the concept refers to the disclosure of financial information. Yin (2009) suggested various tactics to deal with construct validity such as employing multiple sources of evidence. Similarly, the construct validity in this study was enhanced by using the multiple sources of evidence as described in the data collection section. The evidence from the interviews was supported by informal observations, informal conservations people in the organizations, a review of documentary evidence such as published sources in public records (newspapers and information provided on MLAs’ websites), annual reports, monthly management reports, legislative documents, financial reports, etc. In order to enhance the internal validity, data triangulation was performed in which the information from one source was assessed by comparing it to other sources of evidence and interviewing other people (Scapens, 2004).

Establishing a chain of evidence of data is a tactic suggested by Yin (2009). As discussed earlier, all evidence collected such as original tape-recordings of all 26 interviews, soft and hard copy of transcription of interviews, original copies of signed consent forms as well as a register of the time, date and place of interviews and respondent’s profile were recorded and kept in an ordered and coherent manner. Field notes were converted into more formal records once each interview was completed.
5.5.2 Internal Validity

Yin (2009) contends that internal validity is applicable to explanatory case studies and therefore to this thesis. The internal validity is addressed during the data analysis, that is, by the “pattern matching” data analysis method as described by Yin (2009) and cross-case patterns data analysis as described by Eisenhardt (1989). These data analysis methods were described in detail in the data analysis section.

5.5.3 External Validity

The external validity is dealt with by the design of this study itself. This study employs the multiple case research design, whereby all cases were councils from the same industry and relatively similar in functions, activities, and age. Multiple case research design allows a “replication logic”, where the theory is tested through replications of findings in the study and multiple cases should explain a wide range of circumstances. Yin (2009) argues that “once such replication has been made, the results might be accepted as providing strong support for the theory even though further replications had not been performed” (p. 44). However, unlike survey research which relies on statistical generalization, this study does not set out to generalize the findings to a larger context. Rather it is striving to generalize a particular set of results to some broader theory (Yin, 2009).

5.5.4 Reliability

Reliability is promoted by using a case study protocol in which all councils interviewed and all respondents were subjected to the same sequence of entry and exit procedures (Bourgeois & Eisenhardt, 1988). The use of an interview guide assisted in minimizing any errors and biases here (Yin, 2009). In addition, data collection and analysis strategies were clearly explained to provide a clear and accurate picture of the methods used. Additionally, another person reviewed the transcriptions and translations to ensure the correctness and accuracy of the translations to verify the reliability of the evidence found.
5.6 Chapter Summary

This chapter has reviewed the methodological approach followed in this research. It has justified how and why the qualitative case study approach, rather than other methods, fit well into this research. This chapter has further demonstrated the research design, the data collection procedures and methods of data analysis of this research. This study used both primary and secondary data, the former being collected through semi-structured, face-to-face interviews. The case studies were conducted in five local governments consisting of one city council, three municipal councils and one district council. Interview data were collected from twenty-six interviewees such as Head of Finance Department, Assistant Director/Accountant/Valuation Officer, Assistant Accountant, Assistant Internal Auditor and Public Relations Officer. Secondary data were obtained from a review of published sources in public records such as newspapers and websites, annual reports, monthly management reports, legislative documents, financial reports, etc.

Finally, data were analyzed using both manual and electronic methods. In order to analyze the data from the five case studies, the tactics for cross-case patterns were adapted here. The findings are reported in ‘cross-case’ conclusions that incorporate evidence from multiple cases. Both the validity and reliability issues were properly considered in order to ensure the quality of the evidence and research findings.
CHAPTER SIX
FINANCIAL DISCLOSURE DECISION-MAKING

6.0 Introduction

This chapter analyses how decisions regarding financial disclosure are made. The analysis is based on interviews conducted with staff of five Malaysian Local Council case studies referred to as Alpha, Beta, Gamma, Delta and Omega. The respondents’ local authorities are presented in abbreviations as provided in Appendix 6.1. This chapter is organized into two parts. The first part analyses the person/committee responsible for making financial disclosure decisions. The second part analyses how decisions regarding financial disclosure are made.

6.1 Malaysian Local Authorities Internal Structure

Gibbins et al. (1990) emphasize the importance of the internal structure in managing financial disclosure. They state that more disclosure activity happens for a given issue or given disclosure position if certain structures are in place. They defined internal structure as “the extent to which responsibility for the management of the disclosure process is assigned to particular positions within the organization and/or it is guided by clearly understood policies and procedures” (1990, p.133). They underscored the importance of the credibility of a firm’s disclosure position by stating that:

clarity of position and consistency in disclosure behavior are valuable in their own right…credibility seems central to effective disclosure…building the reputation thus requires consistency in behavior within the organization and through time…the consistency is enhanced by having clearly articulated internal policies and by establishing organizational rules and procedures to manage disclosure (p.138).

Gibbins et al. (1992) further state that firms or organizations are organized around certain functions such as marketing, production, accounting, human resource and others. A subunit is defined by these specialities and the presence of specialist subunits is important for understanding how organizational structure may influence disclosure. Specialists tend to identify and solve problems in a manner consistent with their
experience, training and job descriptions. To cite Gibbins et al. (1992) on this theme “the presence of particular specialists in an organization holds the potential to shape the manner in which issues are identified and resolved” (p. 61). From an organizational perspective, what determines whether the organization will manage disclosure activities is the presence of specialist subunits with responsibility for such matters.

Consistent with the above theorisation, local councils in Malaysia are organized around functions and units. Figure 6.1 shows the organization structure of MLAs. Local councils with city status are led by mayors, while municipalities and districts are led by presidents. The state governments, elected every five years, appoint mayors, presidents and all councillors to a three-year term with the option of re-appointment (Section 10 of Act 171). Many of these officials come from the ruling coalition (Phang, 2008a). The Local Government Act (1976) provides for the appointment of not less than eight and not more than twenty-four councillors and a mayor or a president to sit on the full council of a local authority. The mayor or president has substantial influence on how the authority is to be run and he/she is answerable to the state government (Kuppusamy, 2008). The mayor or president exercises executive powers and they are supported by and/or overseen by a system of committees (Phang, 2008a). The mayor or president establishes a number of committees with selected councillors serving as members and presides over council meetings where policies and other decisions (i.e. the appointment of senior council officers including promotion, remuneration and dismissal) are made (Haidar et al., 2004).
Decisions are normally made at the committee level before being brought forward to the full council meeting for endorsement (Kuppusamy, 2008). The councillors normally sit on various committees established to help the local government in management and decision-making. This is stipulated in Section 28 of Act 171. The number of committees depends on local governments’ planning as well as the development plan (Setapa & Lin, 2003). Concerning their functions, they make policy-related and other decisions following recommendations from various committees and assist in the appointment of senior council officers and their employment conditions (Haidar et al., 2004). The existence of the committee in managing the local council was highlighted by most of the interviewees. For example, the Finance Director of Gamma stated:

We have 25 councillors including the President. These councillors are sitting on various committees. One councillor may sit on 3 committees. In Finance Committee, we have 9 councillors as committee members (SSG1).
In lines with the above statements, The Public Relations Officer of Beta stated that they have a total of fourteen committees established in their council to assist them to manage the city council. As shown by her following statement:

The numbers of councillors in Finance committee are twelve including the Mayor. There are a total of twenty five councillors in Beta City Council. Besides the Finance Committee, we also have other committees such as Infrastructure Committee, One Stop Centre Committee, Sustainability Development Committee, Tender Committee and another nine committees. Overall, we have a total of fourteen committees in helping us to manage the council. However, only the Finance Committee is responsible for financial matters (JJB5).

Consistent with Haidar et al. (2004) it seems that the establishment of the committee system is very important in assisting the council in managing the council as well as in expediting their decision-making. In addition, consistent with Kuppusamy (2008), disclosure decisions are normally made at the committee level. The council forms the committees in order to expedite its work. Not all issues need to be brought to the full council meeting as it may delay the decision-making process. Therefore, in order to expedite this process, local government functions are taken up by different committees and most are decided at this level. The issues will then later be brought to the full council meeting generally for the purpose of endorsement only. This is explained by the statement from the Director of Finance Department in Delta as follows:

In local council, we perform a lot of works and categories. So, to do all these jobs, we may have not enough staff and time. Therefore, from the administrative point of view, it stipulated in the Act 171 that the council needs to form the committees. These committees are chaired by the President and under him are the councillors. However, the councillors may sit on several other committees. One councillor may sit on three or four committees. The purpose of these committees is actually to expedite our work and decision-making. This means that we don’t have to bring all issues to Full Council Meeting (LLD1).

To sum up, local councils in Malaysia are organized around functions and units. Executive powers rest with the Mayor (cities) or President (municipalities and districts), supported and/or overseen by a system of committees.
To assist the council in financial management and decision-making, all five selected local councils have established a Finance Committee (in three local councils) or Finance and Assessment Committee (in two local councils). This committee is responsible for financial policies and related issues. All the interviewees claim that their council has established this committee to assist them in these matters. The financial role of the FAC was underscored by the Public Relations Officer of Beta:

In Beta, we have a total of 25 councillors. Twelve of these councillors sit on the Finance and Assessment Committee including the Mayor. Anything to do with financial must be brought to the Finance Committee Meeting. Although some matters are decided in other committees’ meeting, when they come to financial matters, they need to be brought to the Finance Committee Meeting. All matters related to finance including financial policies must be approved in the Finance Committee Meeting (JJB5).

The number of committee members in the FAC varies from one council to another. For example, there are ten councillors sitting on the FAC at Alpha while nine councillors sit on the Finance Committee for Gamma. As explained by the Finance Directors of Alpha and Gamma respectively in their statements below:

We have a committee that we called a Finance and Assessment Committee that is responsible for the council’s financial policy. This committee comprise of ten councillors out of the total of twenty councillors. The meeting must be attended by 3/4 members in order to approve the issues related (KKA1).

Table 6.2 below shows the number of committee members in FAC of the five local councils.

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6 FAC is used to refer to Finance Committee/ Finance and Assessment Committee throughout this thesis.
Table 6.2 Number of Committee Members in Finance Committee/Finance and Assessment Committee

<table>
<thead>
<tr>
<th>Local Authority’s Name</th>
<th>Number of the Finance Committee/the Finance and Assessment Committee members</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alpha</td>
<td>10</td>
</tr>
<tr>
<td>Beta</td>
<td>13</td>
</tr>
<tr>
<td>Gamma</td>
<td>9</td>
</tr>
<tr>
<td>Delta</td>
<td>8</td>
</tr>
<tr>
<td>Omega</td>
<td>12</td>
</tr>
</tbody>
</table>

The interviewees revealed that this committee is generally responsible for approving financial matters and financial policy as well as any changes to the latter. The Finance Director of Alpha states that:

We have a committee that we called Finance and Assessment Committee that is responsible for the council's financial policy…. Basically, the roles of the Finance and Assessment Committee are to discuss and assess the financial issues and to approve the applications related to financial matters. In short, they are responsible for the policies associated with the financial matters and any changes to them (KKA1).

The Internal Auditor of Alpha asserted that the FAC meeting is where the council’s accountants report the financial performance of the council. She commented that:

The Finance Director or accountants report our performance in the Finance and Assessment Committee meeting. They report our monthly as well as yearly performance. They report all financial performance especially on our expenses and revenues. This is required under Section 53 of Act 171 (KKA7).

The Finance Director of Delta explained that one of the functions of the FAC is to approve the accounting treatments or/and financial policies recommended by the external auditors:

Among other functions of the FAC is to approve the treatments and policies that are recommended by the external auditors….If they don’t approve it, we cannot use the recommended treatments and policies (LLD1).
The FAC is also responsible for the approval and endorsement of the financial accounts and budget of the council:

The FAC endorses and approves matters that are related to finance. For example, they endorse the financial statements and budget (AAO2).

The FAC is also responsible for a wide range of financial-related functions according to the Finance Director of Gamma:

FAC is responsible to endorse the budget, financial statements, proposal related to the financial matters such as to make a payment for something; to approve and determine the amount of incentives for the council staff who willing to work overtime for the collection of council’s assessment taxes; and also the approval for the disposal of Assets as well as endorse the financial reports including monthly reports, yearly reports etc. (SSG1).

The FAC is also responsible to make decisions on some other financial issues such as the approval of new assessment taxes, and the approval of property rental extensions. In addition, the FAC meeting is where financial issues such as potential revenues and unexpected expenses are discussed and decided if necessary. As explained by the Assistant Finance Director of Alpha below:

In this council, more than seventy percent of total revenues are generated from assessment taxes and rates. So, if we want to impose assessment taxes in new area, we need to get approval from FAC. Some other issues such as property rental extension; issues related to potential revenues that the council might collect; and issues on unexpected expenses such as expenses on natural disasters are also discuss and decided in the FAC meeting (KKA2).

In summary, the council establishes a FAC to assist in financial management and decision making. The FAC is responsible for financial policies and any issue related to finance such as to approve the accounting treatments, to approve and endorse financial statements and budget and the place where the council’s accountants report the financial performances of the council.
6.2 Financial Disclosure Decision-Maker(s)

Generally, financial management is the responsibility of the Treasury/Finance Department. This responsibility covers all collections, expenditures, payments, budgets and other accounting requirements. This department is also responsible for updating all accounting records and preparing monthly, quarterly and annual financial standing reports and annual financial statements. The interviews revealed that the disclosure decisions are normally authorized at the highest level in the council, consistent with Gibbins et al. (1992). They explained that involving senior people in disclosure decisions implies that the authority for the disclosure decision is high. Gibbins et al. (1992) also provided evidence that significant disclosures and changes in accounting policy must be approved by the committee of senior officers. Similarly, a study by Holland and Stoner (1996) of 27 large UK companies also claimed that voluntary corporate disclosure of price-sensitive information is recognized and authorized at the highest level.

There are two important people or a committee who the interviewees mentioned responsible for making financial disclosure decisions. They are the mayor/president of the council and the FAC. However, financial disclosure decisions lie mostly with the FAC. Similarly, significant disclosures or changes in accounting policy are approved by the FAC that normally chaired by mayor/president, which is the case in all the five local councils chosen for this study. Based on the interview evidence the financial disclosure decision-makers in MLAs are depicted in Figure 6.2.
6.2.1 Roles of Finance/Treasury Department in Disclosure Decisions

Although financial management is the responsibility of the Finance/Treasury Department, in the case of financial disclosure decisions, the interviewees explained that the Director of Finance/Treasury Department normally does not make these decisions as he/she does not have the authority to do so on their own. The Director and accountants may recommend and advise the mayor/president and/or the FAC during the meeting on this matter. For example, Assistant Treasury Director of Delta commented that they in the Treasury Department just implement what has been decided at the FAC meeting. She added that the Treasury Director is not given the discretion to make financial disclosure decisions. She further explained that the Treasury Director and other accountants may only advise and recommend on financial matters at the FAC meeting:

We (Finance Department) just implement and perform what have been decided in the meeting (Finance Committee meeting)….The Treasury Director cannot make financial disclosure decision by his own. We can only recommend and advise on the financial matters in the meeting. We are operating under the supervision of controlling officer. Controlling Officer is the President. The President can make financial disclosure decision based on the advice from the Director of Treasury Department (LLD2).
The above statement is supported by the Assistant Finance Director of Alpha. She indicates that the Finance Director and accountants’ roles in the financial disclosure decision are merely as an advisor to the President and/or to the FAC. They can only provide advice and recommendations but they cannot make any disclosure decision:

We (accountants) advise the committee members (councillors) on some matters that the council cannot disclose to external parties by referring to rules and regulations such as Act 171 and Federal Treasury Circular…The Finance Director and accountants can recommend and advise on the financial disclosure issues in the meeting. However, we (accountants) cannot make disclosure decisions by our own (KKA2).

The Finance Director at Delta further asserted that as financial management is his department’s responsibility, it has the capacity to advise the President and FAC. He claimed that they (accountants) know best when it comes to financial matters and issues:

Financial management is my responsibility. I mean my department's responsibility. In managing the SMC, we have committees. There are numbers of committees. For example, we have Finance Committee…. We do refer to The President when it comes to financial information disclosure. In fact, in certain situations, the President comes to us and seeks our advice whether or not to disclose some financial information. Put it this way, we actually know what to disclose and what not to disclose….. We have the capacity to advise the President because financial management is our responsibility (LLD1).

Sharing similar views, the Assistant Finance Director of Beta commented that the FAC is very co-operative and most of the time they do not have any problem accepting the recommendations and advice from accountants pertaining to financial disclosure. It is accepted as long as they follow the established procedures (e.g. Act 171, Federal Treasury Circular etc.):

We need first to get approval from the Finance Committee and the Mayor, who normally sit in the Finance Committee to disclose anything in our financial statements. Most of the decision regarding the disclosure of financial information are decided in this committee meeting….I must say most of the time the management and the Finance Committee do not have much problem on what we want to disclose. They are very co-operative as long as we disclose the information in line with the established procedures (JJB1).
To sum up, the Finance/Treasury Department is responsible for financial management of the council. Although financial management is the responsibility of the Finance/Treasury Department, the Director of Finance/Treasury Department does not make the financial disclosure decisions as he/she does not have the authority. However, he/she and other accountants may recommend and advise the Mayor/President and/or the FAC in regards to financial disclosure issues during the meeting.

6.2.2 Roles of Mayor/President in Disclosure Decisions

It appears from the interviews that mayors and presidents played significant roles in making financial disclosure decisions. Consistent with the claims by Kuppusamy (2008), Phang (2008a) and Haidar et al. (2004), they have the authority to make these kinds of decisions. The interviewees claimed that he/she is the “controlling officer” of the council. As such, he/she is responsible for the local authority’s income and spending. Further, Section 10(7) states that if the mayor or president does not agree with the other councillors on certain decisions, he/she can refer them to the Chief Minister or the ‘Menteri Besar’ of the state whose decision is final and binding. The Act 171 gives mayors or presidents a substantial influence on how the local authority is to be run, including financial management and disclosure practices of MLAs. It is confirmed by following statement by the Internal Auditor of Alpha:

The President as a Controlling Officer must know all information in the council. We need first to inform or disclose any information to him. His decision is crucial. He has the power to make decision even though the decision is made by him alone. However, I must say that our President normally exercise his discretion and take into consideration of others’ point of views and opinions. Especially when it comes to financial information disclosure, he normally seeks advice from the Director of Finance Department (KKA7).

In addition, the involvement of the mayor/president in financial disclosure decisions seems to be more critical when the issues are associated with sensitive issues. However,

7 The Finance Minister or the Menteri Besar or Chief Minister, as the case maybe, may appoint, in respect of each purpose of expenditure provided for any financial year in the estimates, a controlling officer to control, subject to any directions given by the financial authority, the expenditure authorized under that purpose and to be the chief accounting officer in respect of all public moneys collected, received or disbursed and all public stores received, held or disposed of by or on account of the department or service for which the purpose is provided (Sec. 15A, Financial Procedure Act 1957).
the extent of these issues is not clear as the interviewees were reluctant to discuss them in detail. The Assistant Director of Delta claimed that the decision to disclose financial information is in the hands of their president especially when the information concerns “sensitive” information:

In reality, the head of accountant for the local council is actually Mr. President. The Federal Treasury Instruction (FTI) states that the accountant need to get approval from the President on whatever he/she wants to disclose. In Financial Procedure Act 1957, the President is the “controlling officer” of the council. In the local council context, The President is responsible to make financial disclosure decision. The approval is in the hand of President. The reason here is that he is the controlling officer cum head of the local council. The decision what to be disclosed in the President’s hands, especially when it comes to the “sensitive issues (LLD2).

The mayor/president is exercising extra caution in disclosing financial information especially “sensitive” financial information as it may have implications to the community. He/she fears that the information can be wrongly interpreted by difference levels and backgrounds of the public. The Finance Director of Omega said:

In local council, we to give extra attention to the politics and community issues. Actually, “by book” we need to disclose all financial information to the public from A to Z because we are handling the public money. In reality, however, before we disclose any financial information, we need to get the President’s approval… In the book, once we got the audit report, we can disclose everything. However, in actual practice, if we do so, it may have the implication to community, because our community has difference education levels and backgrounds and that information may be interpreted differently by the public (AAO1).

Furthermore, the mayor/president is exercising extra caution in disclosing “sensitive” financial information as it may also have implications to the current state government. The Finance Director of Omega added:

We need to be sensitive to the current ruling government. This is because whatever we disclose, it gives the implication not only to us, but the state government as well….To be straight to the point, the main issue here is politic sensitivity. Certain financial information can be sensitive issues or can be a target for the opposition party. Giving this scenario, our Controlling Officer (President) is more cautious in disclosing any “sensitive” financial information.
To some extent, we only disclose financial information in general not in detail (AAO1).

The Finance Director of Alpha claimed that not all financial information is disclosed to the councilors especially the “sensitive” information. She said:

We don’t disclose everything to the councillors. To be frank, we don’t disclose all of financial information especially when it is associated with the “sensitive” information. If the information is just a normal monthly updates, we normally have no problem to disclose it as it is always according to standards and regulations. However, some information that we treated “private and confidential “… we normally don’t disclose them (KKA1).

Further, she claimed that not all information details are disclosed to the councilors because they believe not all of them can understand a lot of detailed information:

We don’t really disclose the details to the councillors because we believe that sometimes they don’t know how we carry out our duty or task. Furthermore, their appointment is temporary for the period of 2 to 3 years only. Therefore, they are not permanent personnel in the council (KKA1).

The Finance Director of Alpha gave an example for her claim. One reason why the council does not disclose all financial information to councillors is to avoid conflict in decision making. She said:

…for example, in the case of our fixed deposits. Our fixed deposits are supposed to be deposited in the local bank. However, upon making a market comparison between banks, we found out that the foreign banks offer higher interest rate. If we disclose this to the councillors, we worry that this will cause conflict (KKA1).

Further, the reason why the council does not disclose all financial information to councillors is to avoid conflict of interest among councillors:

…or worse case scenario they direct us to deposit the money to the bank that they preferred….There are justifications for these actions, for example, as a Muslim; we normally prefer Islamic banking than conventional bank. If we put the money in the conventional banks, we worry that the source of dividends or
interests we earn are incredulous. Furthermore, we are dealing with public money (taxpayers) (KKA1).

Another reason as evident from the comment of The Finance Director of Alpha is to expedite the decision making process. She added:

In addition, if we disclose this to the councillors in the FAC meeting; we would get lot of different opinions. We have ten councillors with different views and opinions. At the end of the day, we would confuse and this makes our decision-making process difficult. Sometimes, the councillors have some corporate interest that make them in favor for certain banks. Therefore, we worry of favoritism….For this kind of situation, we just bring this matter to the President and get his approval to deposit our money to the local banks and support our local banks. He will give us the written approval. By doing this, we believe that it eases our task and expedites our decision-making process (KKA1).

Therefore, the interviewees’ evidence suggested that before the financial information is disclosed to other internal or external stakeholders, the Finance/Treasury Directors are normally first to bring them to the mayor/president for advice and consultation. The interviews revealed that mayors and/or presidents have the authority to make financial disclosure decisions and it is more evident when a financial disclosure decision is associated with political and “sensitive” issues. Further, the interviews suggested that not all financial information is disclosed to the councillors.

6.2.3 Roles of the Finance Committee/Finance and Assessment Committee in Disclosure Decisions

The involvement of the FAC in making disclosure decisions were raised by most interviewees who claimed that the financial disclosure decisions are normally made at this committee level. This is consistent with Kuppusamy (2008) who stated that the decisions are normally made at the committee level and later brought to the full council meeting for endorsement. Kuppusamy (2008) also claims that, in practice, most councillors will not challenge the decisions that have been made at the committee level and this practice is commonly accepted by them. The interviewees revealed that the financial matters such as disclosure decisions need to be approved by this committee.
For example, the Finance Director of Omega remarked that financial issues need to be decided at the FAC meeting:

> We have Financial and Assessment Committee in the council. It is my responsibility to inform this committee regarding the financial position and performance of the council. Issues related to financial disclosure need to be tabled and decided in the Finance and Assessment Committee Meeting (AAO1).

Similarly, the Assistant Treasury Director of Beta also claimed that the FAC is responsible for approving the financial disclosure decision. She added that the FAC is a policy-maker and she further claimed that for any revenue or expense they want to disclose, they need to bring it to the FAC meeting for approval:

> The Finance Committee involves in the financial disclosure decision. This committee approves the decisions. This committee is a policy-maker. They approve our financial statements and budget....As I said, issue related to financial matters need to be brought to Finance and Assessment committee meeting. If we want to disclose whatever revenue or expenses, we need to be present and get approval in this meeting (FAC). This committee is very important. I would say this committee is the main committee for financial matters (JJB2).

The Director of the Internal Audit Unit of Beta added that the FAC meeting is where the financial regulations, procedures and policies are reviewed and decided:

> The Finance Committee meeting is where the financial regulations, procedures and policies are reviewed and decided. This includes the decisions on financial disclosure (JJB4).

Similarly the Treasury Director of Beta asserted that, although she is the Treasury Director of the council, she does not have the authority to make financial disclosure decisions. Financial matters including financial disclosure decisions are made by the FAC:

> I don’t have the authority to make financial disclosure decision. Disclosure of new income or expenses, if any, is approved by the Finance Committee during the budget preparation. All other things which are not in the budget need to be
approved by the Finance Committee. For those expenses which are approved in the budget, there is no issue. For those expenses which are not in the budget, they must be approved in the Finance Committee Meeting and must be endorsed in the Full Board meeting. As I said earlier on, anything that related to money and financial matters including financial information disclosure need to be approved by Finance Committee (JJB1).

The Assistant Treasury Director of Delta added that most of the financial disclosure decisions are decided in the FAC meeting. She further claimed that the president as a chairman of the FAC and the controlling officer of the council may exercise his discretion on financial disclosure decisions during the FAC meeting:

I must say that most of the financial disclosure decisions are decided in the Finance Committee meeting. In other words, the matters are actually needed to be tabled, discussed and decided together in the Finance Committee meeting. In this meeting, The President as the chairman of the committee and as a Controlling Officer of the council can exercise his discretion (LLD2).

Consistent with Haidar et al. (2004), the above statements reveal that the Finance Committee is responsible for debating and approving the financial disclosure decision. Similarly, Haidar et al. (2004) also assert that the policies of the council are normally discussed and approved at the committee level. In line with this, the FAC is given the authority to approve the accounting policy and any change in the accounting policy in MLAs. The policy can only be applied after it has been approved by this committee. For instance the Accountant of Omega stated that the FAC of their council is responsible for approving the accounting policy based on the recommendation and advice from the accountants, particularly emanating from the Treasury Director:

In helping us to manage the financial matters, we do have the Financial and Assessment Committee in the council. Normally, anything related to financial matters need to be brought to the FAC meeting. They need to approve every decision we want to make. They approve on the accounting policy (s) as well based on the recommendation and advice from the accountants, particularly the advice from the Treasury Director (AAO2).

The accountants of the MLAs also acknowledged that the councillors those on the FAC.
This is illustrated by the comment from the Assistant Director of Beta below:
The Finance Committee involves in the financial disclosure decision. This is the committee that approves the decisions. This includes the approval accounting policy. This committee is a policy-maker. They also endorse and approve our financial statements and budget (JJB2).

Similarly, any changes in accounting policy need to be approved by the FAC. As commented by the Finance Director of Alpha below:

The FAC is very important in our council because they involve in financial policy and financial matters. The Finance committee meeting is attended by councillors. Councillors are decision-maker. Meaning they are also a policy-maker. Proposals and papers related to finance need to be presented in the FAC meeting for approval. This includes any recommendation on the change in accounting policy. Again, I would say that this committee is a policy-maker. We cannot simply overrule their decision. Therefore, they are very strong and we refer to them before we disclose any financial matter (KKA1).

The Assistant Director of Delta added that only approved accounting policies can be used and applied by the council. She further added that even though the accounting policies are advised by the AG, they need to be tabled and approved at the FAC meeting:

Any change in the accounting policy as a result of the External Auditor advice need to be tabled and approved in FAC and be treated as new accounting policy. This means that we are not fully bounded by the Federal Treasury Circular. Any policy needs to be approved. Only approved policies can be applied. Normally, changes in the policies and accounting treatments are based on advice from the appointed external private auditor and Auditor General (LLD2).

The interviews also reveal that the policies of the MLAs must be in line with federal and state government policies. Under Item 4 in List II of the Ninth Schedule of the Federal Constitution, local government is a subject under the State list, with the exception for the federal Territories of Kuala Lumpur, Putrajaya and Labuan (Kuppusamy, 2008; Phang, 1997). Therefore, the state government has the power to determine the programs and policies suitable for the local government. Although local government is under the state list, through the NCLG, a consultative body set up under Article 95 (A) of the Federal Constitution, the federal government can influence local government. The NCLG can formulate policies and advise the state government on
matters pertaining to local government. The policy decisions made at the NCLG bind all state governments, except Sabah and Sarawak who are invited to the NCLG on an observer status. One of the functions of NCLG is to ensure uniformity of policies and conformity to rules and regulations for local government with the exception of Sabah and Sarawak. This also means that the NCLG’s position at the federal level is to ensure state and local governments follow the national policies:

We in the local council are empowered to draft the policy. That is why we have the councilors. Any change in accounting policy is approved in the FAC meeting. Besides that, this committee approves and come out with new policy that is not contradicted with the state and federal governments’ policy (AAO1).

Therefore, in line with Kuppusamy (2008) and Haidar et al. (2004), the Finance Committee is not only responsible for making financial disclosure decisions, they are also responsible for approving accounting policy as well as any changes to it. As claimed by the interviewees, they are not only decision-maker, they are also the policy-makers.

In summary, the interviews revealed that the mayor/president is given the authority to make some financial disclosure decisions. They have the right to make some financial disclosure decisions based on the advice received from and discussion with accountants, particularly Finance/Treasury Director. The mayor/president’s discretion in financial disclosure decision-making is clearly evident when this is associated with political and “sensitive” issues. However, the interviews also reveal that most of the financial disclosure decisions are made by the FAC which is normally chaired by the mayor/president, which is the case in all the five local councils chosen for this study. The FAC also approves of the financial policy of the council.

### 6.3 How Decisions Regarding Financial Disclosure are Made

Some of the respondents revealed that some financial disclosures are decided based on meeting with the mayor/president. For some financial disclosure issues, the Director of the Finance Department/Treasury Department just need to inform and consult the mayor/president and he or she agrees to do so. Issues are decided in that meeting and
brought to management generally for more information. For instance, the Treasury Director of Delta claimed that some disclosure issues such as fixed deposits decisions are decided after, meeting with the president for approval:

For fixed deposits decisions, we just need to notify and consult the President. Sometimes, things are decided there if the President gives the green light (LLD1).

Similarly, the Treasury Director of Gamma claimed that some financial disclosure decisions are decided by the president based on her advice in one-to-one meetings:

For some financial disclosure decisions, I normally not bring them to the FAC meeting. It is our routine for that kind of practices. I am talking about some financial disclosure decisions. The decision is based on the President’s decision. If the President says ok, then I just follow that….These decisions are brought to management meeting for information and notification (SSG1).

The interviews also reveal that the normal process of deciding financial disclosure is through the management and FAC meetings. For example, the accountant working at Delta asserted that financial disclosure decisions are done in this way. The accountants can recommend and advise the councillors on disclosure issues. However, decisions are decided by the committee members in the meeting:

Most of the financial disclosure decisions are decided in the meetings. I mean the meetings with the management and councillors. Generally, the disclosure decisions are decided in the Finance Committee Meeting and endorsed in the Full Council Meeting. The accountants can recommend and advise any change in the financial disclosure practice or policy in the meeting. However, the decisions are made in the meeting (LLD3).

The accountant working at Alpha added that the normal process for financial disclosure decision-making is by bringing the financial issues to the management meeting first and then to the FAC meeting. She added that the financial disclosure issues are normally decided here:
The Finance Director then brings the financial disclosure issues to the management meeting and subsequently to the FAC meeting. Normally, the process is like that. Things are decided there (in the meetings) (KKA3).

Similarly, the Finance Director of Alpha elaborated more on the financial disclosure decision-making process, explaining that issues are normally decided at the management and FAC meetings. He said:

The financial disclosure decisions are normally decided in the management meeting and Finance and Assessment Committee Meeting (KKA1).

However, he claimed that for those financial matters that are decided by the president alone based on the discussion and advice from accountants, these are not normally brought up at meetings. As discussed earlier the financial matters are decided by the president in his or her capacity as controlling officer of the Council, as claimed by the interviewee. He added that for those financial issues that are to be brought to the FAC meeting, they normally discuss them first in the management meeting. He further explained that although the management meeting agrees on certain financial issues, the FAC decisions can overturn them if the FAC meeting failed to reach consensus:

For those financial issues that are decided by the President as I mentioned earlier on, we normally do not bring them to these meetings...Whatever matter that has been discussed in the FAC meeting, we normally discuss it again in the management meeting. Normally, the discussions are based on how we can improve our practices after the feedbacks we received in the FAC meeting.....Normally, before we bring the financial matters to the FAC meeting, we present them first in the management meeting. However, the decision to disclose financial information is always with the President and the councillors during the meetings. Although the management meeting agreed on certain financial matters, for example, to disclose new expenses or revenue, this agreement is void if during the FAC meeting the councillors failed to reach a consensus and approve it. The councillors are the policy-maker. Therefore, they have the power. If 3/4 of the councillors disagree with certain matter, automatically the decision made by the management is void (KKA1).

As mentioned earlier some interviewees strongly acknowledged the importance of the FAC meeting in deciding and approving the financial disclosure decisions. They revealed that these decisions need to be tabled, discussed and approved in the FAC
meeting. Some financial information cannot be disclosed if the FAC does not give its consent. For example, the Public Relations Officer of Beta asserted that the financial disclosure issues are normally tabled, discussed and decided on at the FC meeting:

Basically, the financial disclosure decisions are decided in the meeting. I am talking about the Finance Committee meeting. Financial issues are tabled, discussed and decided on at the FC meeting. That is how financial disclosure decision is decided (JJB5).

Similarly, the Finance Director of Omega explained that the financial disclosure issues are normally discussed and debated in the FAC meeting, which is where financial issues are decided. FAC meetings are attended by all heads of departments and the Finance Department as a secretariat. As such the debate and discussion at this meeting receive more opinions and advice from various experts. However, it is only the FAC members who can decide and vote. If the FAC meeting fails to reach a consensus on certain financial disclosure issues, the president will use the voting system to his or her discretion if there is a 50-50 split:

The financial disclosure issues are discussed in the FAC meeting. The meeting is led by the President. The meeting is attended by 12 councillors who sit on this committee. The financial disclosure issues are debated and all implications they may caused to the council and the state government are discussed. The meeting is also attended by all heads of departments because they also give information from their departments during the meeting. Therefore, once the issues have been debated and discussed by various people who come with various expertise and experiences, the matters then decided. The expertise and experience do help during the debate and discussion. The decision may be either yes or no. If yes, then we can disclose the financial information. If the answer is no, then the minutes of the meeting will record that the matter or issue cannot be disclosed. If happened such as a 50-50 situation, then the chairman may have to do the vote. The FAC is very important to the council. I may say that they are a decision-maker (AAO1).

The Assistant Treasury Director of Beta commented that their Finance Committee is aware of the Federal Treasury Instructions and Treasury Circular. The accountants working at MLAs make use of Federal Treasury Instructions and Federal Treasury Circular when preparing their financial statements and budgets. She added that at the FAC meeting they table and receive the approval for any policy that they want to
implement. She further asserted that no financial policy can be enforced or adapted without approval from the FAC:

The Finance Committee is aware of Federal Treasury Instructions and Circular. By right, they must aware of these because they sit on the Finance Committee. Furthermore, the FC meeting is the place where we present all circulars that related to financial matters that we want to adapt. As I mentioned earlier, for example, if we want to enforce the policy such as TI no. 59 (a), we need to present it first in this meeting before we can enforce them. We cannot enforce or implement anything without approval from the committee. We need to get the approval from the Finance Committee Meeting and the matters are endorsed in the Full Council Meeting. This applies to the financial disclosure decision as well. They must be decided in this meeting (Finance Committee Meeting). We have both meeting once a month (JJB2).

As explained by the Assistant Treasury Director of Beta, the management and FAC meeting is held every month:

The council has both the management and FAC meeting in once a month (JJB2).

As for the quorum of the FAC meeting, the Finance Director of Alpha explained that the meeting is valid only if it is attended by 3/4 of the committee members.

The FAC meeting is valid if it is attended by ¾ of the committee members (KKA1).

In summary, the interviews revealed that most of the financial disclosure decisions are normally tabled, discussed and approved in the FAC meeting before these matters are brought to the full council meeting to be endorsed. The interviews also revealed that some financial disclosure issues are decided in one-to-one meetings between accountants, particularly the Finance/Treasury Director and mayor or president. The accountants, particularly the Finance/Treasury Director normally play a role as an advisor at these meetings.
6.4 Chapter Summary

Financial disclosures are authorized at the higher level within the local government. The interviews revealed that the mayor/president and FAC have the authority to make financial disclosure decisions. Although financial management is the responsibility of the Finance/Treasury Director and his/her department, he/she has the capacity as an advisor only and can only recommend to the mayor/president and FAC during the management and FAC meetings. The FAC has the authority to approve accounting policies and any changes in them based on advice from the Finance/Treasury Director. No policy can be adapted or applied without the consent of the FAC.

Financial disclosure is decided in several ways. Several interviews revealed that it is decided at one-to-one meetings between accountants, particularly the Finance/Treasury Director and the mayor/president. The decisions are then brought to management meeting for information and notification. The interviews revealed that not all financial disclosure issues are brought to the FAC meeting. Some financial disclosures are decided by the mayor/president with the advice of Finance/Treasury Director at the management meeting. They revealed that some financial matters are not appropriate to be brought to the FAC meeting are decided by the mayor/president only. This person’s involvement in the financial disclosure decision seems to be more crucial when the issues are politically sensitive. The mayor/president is the key person in the financial disclosure decision as claimed by several respondents because he/she is the controlling officer of the council. Furthermore, he/she is also the committee member of the FAC but most interviewees asserted that financial disclosure issues need to be tabled, debated and approved at the FAC meeting.

The existence of these structures in the local council influences disclosure. From an organizational perspective, the presence of Finance/Treasury Department, The Controlling Officer (the mayor/president) and the FAC with responsibility for disclosure matters determine how the organization manages disclosure activities.
CHAPTER SEVEN

MEDIUM OF DISCLOSURE AND THE REASONS FOR DISCLOSING INFORMATION

7.0 Introduction

This chapter reports findings from interviews with the intention of answering the second research question: How does the organization disclose financial information and why does it do so? This chapter is organized into two parts. The first part analyses how MLAs disclose their financial information. This part includes analysis about to who it is disclosed, the frequency and adequacy of disclosure and the analysis of data content and data organization in their financial statements. The second part analyses why the MLAs disclose the financial information.

7.1 Medium of Disclosure

Gibbins et al. (1992) state that financial disclosure can be done through a variety of media or channels. These channels or medium include “official written documents such as annual reports or securities filings, news releases, electronic data transfers, speeches, phone calls, and announcements over news wires…” (1992, p.19).

Table 7.1: Medium/Channel of Disclosure

<table>
<thead>
<tr>
<th>Medium/Channel</th>
<th>Number of Interviewees (A total of 22 interviewees answered the question)</th>
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<tbody>
<tr>
<td>Financial Statements</td>
<td>19</td>
</tr>
<tr>
<td>Budgets</td>
<td>18</td>
</tr>
<tr>
<td>Monthly reports</td>
<td>14</td>
</tr>
<tr>
<td>Annual Report</td>
<td>11</td>
</tr>
<tr>
<td>Website</td>
<td>8</td>
</tr>
<tr>
<td>Speeches</td>
<td>7</td>
</tr>
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Table 7.1 shows the medium/channel of financial disclosure in MLAs. Generally, the majority of the interviewees are able to identify the medium of financial disclosure. In general, there are six medium/channels of disclosure mentioned in the interviews.
Twenty-two interviewees responded to this question. Another four interviewees were unable to answer it for some reasons such as being outside their responsibilities and having only little knowledge on the medium/channel of disclosure. It is apparent from this table that financial statements and budgets are the two main mediums for financial disclosure. Further, monthly reports, annual reports, websites and speeches are also mentioned by the respondents as the mediums for financial disclosure in MLAs. The respondents mentioned that the monthly reports normally consist of Expenses Statement Report, Revenue Statement Report, Fixed Deposit Statement Report, Accrued Assessment Revenues Report, and Cash Flow Report. This is indicated by the following statement by the Finance Director of Alpha below:


The respondents revealed that the annual report is not the main medium of disclosure in MLAs. Consistent with Mack and Ryan (2007) and Hassan, Hassan and Nor (2007), not all MLAs prepare an annual report since it is not mandatory. Instead it is prepared by MLAs which can afford to do so in terms of having the money and staff. When asked for a copy of an annual report, only three out of five MLAs did so.

Even though the interviews were conducted in 2010, two councils gave a copy of the 2007 annual report and another council provided a sample of the 2006 annual report. This suggests that the annual reports of those local councils are outdated and this problem was acknowledged by Director of the Internal Audit Unit of Beta:

Actually, we are having technical problems in producing and releasing the annual report for the past two years. Therefore, we use audited financial statements and budget as a medium of disclosure. They are current and updated (JJB4).

A scan of the lobbies or counters of the five councils selected for the study revealed that none of them display audited financial statements, budgets or annual reports. This suggests that these documents are not accessible to the public. Similarly, when asked for a copy of the annual report, the release of the copy of annual report of two of the councils was subject to approval from senior management. The interviews also revealed that the council website has not been used extensively as a medium for financial
Financial disclosure online is totally voluntary in MLAs and only practiced by councils that have sufficient information technology (IT) facilities and adequate specialized staff (Ghani and Said, 2010). Out of the five local councils selected only two disclosed their financial information online. This is consistent with the study carried out by Ghani and Said (2010) on 109 MLAs which found that only 64.2% of local governments maintain websites and only 15.7% of local governments disclose financial information digitally.

In this study the Beta council has disclosed their annual reports from 2006 to on their website. This council has also disclosed its audited financial statements from 2005 to 2009 as well as their budget speech for 2008 and 2009 online. With regards to financial information disclosure, this council claimed that it is very open to the public, especially to the community who live in its administrative area as claimed by the Finance Director of Beta. She added that this is acknowledged by the Ministry of Housing and Local Government and that they even share the future plans of the council with their residents:

Our council is considered very open to the public with regards to the financial information. This is certified by the Ministry of Housing and Local Government itself. As compared to other councils, we are very open. We do disclose our financial information in our website…. We disclose our annual reports, audited financial statements and budget in the website….. The residents normally aware of what we are planning for them (PJB1).

As for Omega council, the interviews revealed that it only provides the financial budget (A summary of Revenue and Expenses Projection for 2010 and 2011) on their website. They claimed that they purposely disclose no details or too much information in the website so that the information can be understood by the public. As revealed by the following comments by Finance Director of Omega:

We disclose our budget in the website. So, here, the information is accessible to everyone including the public. However, nothing much we disclose there. Basically, it is a summary of financial budget for our revenues and expenses only. As you can see, it is a summary of revenues and expenses projection for the year of 2011 and 2012. We purposely do not put too much information or too many details because we knew that the public might not be able to read them (AAO1).

Finally, the interviews revealed that financial disclosure is done through speeches, which refer to the speech and budget speech by the mayor/president at the full council
meeting. During the meeting and budget speeches, the council invites the media and press to attend. For example the Treasury Director of Delta commented that their council normally invites the press to their full council meeting. He asserted that the press represents the public as they report the information in the newspapers, including financial details disclosed in the full council meeting. He further added that the press is normally aware of their financial information because it is always disclosed at the full council meeting especially in the president’s speech:

We invite the Press to our Full Council Meeting. I think this is another way to disclose the financial information to the public. The Press represents the public and I consider the information has been disclosed to the public from time to time. As the meeting is always attended by the press, they know about our budget and financial information. Normally, we do disclose financial information in the Full Council Meeting. After the meeting, we normally have a press conference. During this time, the reporters ask many questions especially on the issues reflecting from the President’s speech during the meeting (LLD1).

Notably, the full council meetings of the other four local councils are also attended by the press. Thus all the interviews revealed that every council invites the press to a full council meeting.

7.2 To Whom They Disclose Financial Information

There is a huge body of literature on the actual and potential users of public sector reporting. For example, Pilcher and Dean (2009) state two types of reports in which financial information is normally provided by local government. These are internal financial reports which are usually disclosed to managers and councillors, and external financial reports which are normally disclosed to external stakeholders like ratepayers, the relevant minister and government department or agency.
Table 7.2: Stakeholders of Financial Information

<table>
<thead>
<tr>
<th>Stakeholders</th>
<th>Number of interviewees (A total of 22 interviewees answered the question)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Internal Stakeholders</strong></td>
<td></td>
</tr>
<tr>
<td>Councillors</td>
<td>22</td>
</tr>
<tr>
<td>Management</td>
<td>22</td>
</tr>
<tr>
<td><strong>External Stakeholders</strong></td>
<td></td>
</tr>
<tr>
<td>State Authority</td>
<td>22</td>
</tr>
<tr>
<td>Auditor</td>
<td>18</td>
</tr>
<tr>
<td>Ministry of Housing and Local Government</td>
<td>14</td>
</tr>
</tbody>
</table>

In the case of MLAs, the interviews revealed that the local councils normally disclose any financial information to the management, councillors, state authority, auditor and the Ministry of Housing and Local Government as shown in Table 7.2. These stakeholders can be classified into internal and external stakeholders (Atamian & Ganguli, 1991; Mack & Ryan, 2006, Pilcher & Dean, 2009). Out of twenty-two interviewees who responded to the question, all of them mentioned that they disclose financial information to the management, councillors and state authority. In addition, the MLAs also disclose financial information to the auditor and to the Ministry of Housing and Local Government. For instance the Treasury Director of Beta commented that they disclose financial information internally such as to management and councillors. They also disclose financial information to external parties such as the auditor and state authority:

*We disclose the financial information up to the councillor level. Internally, we disclose the financial information to the management and all the councillors. Externally, we do disclose financial information to the Auditor as well as to the state authority (JJB1).*

The financial information disclosure to the mayor/president and councillors is required by the Act 171. For example, Section 53 of Part VI of the statute states:

*The local authority shall cause proper books and accounts to be provided and true and regular records to be entered therein of all transactions of the local authority and such books and accounts shall be open at all reasonable times and*
Similarly, the disclosure to the state authority is also provided in the Act. For example, Section 60 (5) of Part VI states that “A copy of the statements and accounts shall be forwarded to the State Authority which shall cause it to be laid on the table of the State Legislative Assembly and, in the case of the City of Kuala Lumpur, of the House of Representatives”. For the disclosure to the Auditor, it is stipulated under Section 60 (1) of Part VI of Act 171. The Section states that: “The Auditor General or other auditor appointed by the State Authority on the recommendation of the Auditor General shall, throughout the financial year, inspect and examine the accounts of the local authority, and the local authority shall, by the Treasurer or other officer authorized by the local authority, produce and lay before the auditor all books and accounts of the local authority together with all vouchers, papers, contracts and documents relating thereto.”.

However, the disclosure to the MHLG is normally done on the ministry’s request. For example, the Finance Director of Omega commented that they only provide financial information to the MHLG when the ministry asks for it. She further added that the MHLG normally requests the financial information to the state authority, not directly from the council

…we only disclose to the Federal Government when they request them (financial information). Normally, the request is made by Ministry of Housing and Local Government (MHLG). They normally request the information when they want to do the case study, to answer the question from Senate or National Hall and maybe for grant purposes. However, they normally request the information from the State Government, not directly from us (local council). We disclose our financial information to the state authority on monthly basis. Therefore, they (state authority) have all of our financial information. That is why they (MHLG) normally request the information from the state authority (AAO1).

The above comment is supported by the comment from the Treasury Director of Alpha, who commented that the MHLG seldom asks for financial information:

Sometimes we disclose financial information to Federal Government, MHLG to be exact. However, the MHLG seldom asks for our financial information. We only provide information to the MHLG by request (LLD1).
Although the study of 305 taxpayers in three MLAs by Tayib et al. (1999) revealed that more than 88% of the taxpayers desired local government financial information be made available or disclosed publicly, the interviews revealed that there is no direct financial disclosure to the public just yet in the MLAs’ disclosure practices, with the exception of website disclosure. As claimed by Finance Director of Alpha, they never disclose their financial information publicly. He added that there is no reason for them to do so and they do not have an intention to do so in the future. He explained that this is because some parties may misuse this financial information:

We never publish our financial information directly to the public or at a public place. There is no reason for us to do that. We also don’t have any intention to do so….In council opinion and in my opinion, the reason behind that is that we fear of misinterpretation of our financial information. Not everyone knows how to read the financial information and we fear that other parties will misuse the information (KKA1).

However, Beta Council and Omega Council are more open with their financial information and they have published it on their websites. If the public would like to access the financial information of these two councils, it is available on line. However, this needs to be approved and audited before such data is made available digitally. For example, the Finance Director of Beta commented that they publish their financial information on the council’s website in order for the public to be informed of the council’s position and performance as well as the council’s plans for their communities:

We publish in the website so that the public especially the taxpayers will be able to see our financial information. From the information, they will be able to see what our current position and performance. They also will be able to know what we plan for the coming years…However, the information need to be approved and audited before we can disclose them (JJB1).

The interviews also revealed that the audited financial statements of the MLAs are published in the official government gazette, as stipulated in Section 60 (4) of Act 171: “The audited accounts together with the auditor's observations thereon shall be laid before the local authority at its next ensuing ordinary meeting and shall be published in the Gazette”. For example, the Treasury Director of Beta commented that the audited
Once the audit certificate is issued, that means the financial statements are audited and finalized. The financial statements will then be gazette in the official government gazette and we can publish the financial statements in the website (JJB1).

However, Tayib et al. (1999) found that the public had no access to the financial information published in the official government gazette because they were unaware of its existence.

In summary, it is apparent from the interviews that the local councils in Malaysia disclose their financial information not only to internal parties, but externally as well. However, public disclosure is still limited as only two out of five local councils disclose their financial information on their websites.

### 7.3 Frequency and Adequacy of Financial Disclosure

With regard to the frequency of such disclosure, all the interviewees who responded to the question mentioned that they disclose financial information to the management, councillors and state authority on a monthly basis. For auditing reasons the interviewees informed that they disclose financial information on a yearly basis, as indicated by the following comment from Director of Treasury Department of Beta:

> We disclose financial information on a monthly basis to management, the councillors and to the state authority. For the state authority, we need to send the report to them by 10th day of every month. By or before 30 April, we need to disclose or submit the financial statements to the auditor for auditing purposes (JJB1).

For the federal government (MHLG), the interviews revealed that they only send the audited financial statements if the MHLG requests it. This indicates that the MLAs are not required to disclose their financial information to the federal government unless requested to do so and it is not mandatory. Additionally, it seems that the main recipients of the financial information of local councils are management, councillors and state authorities as well as the auditors.
With regard to the adequacy of the financial information disclosed, all of the interviewees (ten interviewees) who responded to this question claimed that they are satisfied with the financial information they provided. They claimed that they have provided enough detail to the users of financial information, as indicated by the following comment by the Assistant Director of the Treasury Department of Beta:

I think we have provided them with sufficient information. So far, we have never received any complaint saying that they are not satisfied with the information we provided. For the public, we are more transparent nowadays. Though we don’t disclose all financial information to them, we have not yet received any complaint stating that they are not satisfied with the information we disclose to them (JJB2).

Similarly, the Finance Director of Omega is satisfied with the level of financial information that the council provides to users. She added that different target audiences required different levels of financial information, and if they provide too much detailed information, the target audiences may fail to understand what it means:

I am satisfied with the level of financial information we provided. I think we have provided adequate information and disclosure. I must say different audiences may require different level of information and I believed that if we disclose too details, not everyone will be able to understand and use the information. Whatever it is, it is depend on the target audience. For the public, we purposely not to put too much information or too many details because we knew that the public may not be able to use them (AAO1).

Furthermore the Director of the Internal Audit Unit at Beta confirmed the above statements by commenting that their council has provided sufficient disclosure of financial information. He added that, for the public, especially the taxpayers, their main concerns are good services and better facilities:

I think the financial information that we disclosed is sufficient. Unlike the corporation which operating with profit maximization motive, we in the local council are operating to provide social services. This means that we are operating without profit maximization motive. The corporation will give the investors the dividend. In local council, we are giving back to community by providing them with good facilities and services. Basically, these are the differences between local council and corporation. The taxpayers concerned are mainly on what returns they get from what they have paid. The returns are normally in form of good facilities and services. For example, they expect us (local council) to provide them with city beautification, with good road
conditions, provide them with markets and good drainage system and other things. Basically, these are their main concerned (JJB4).

To sum up, the MLAs disclose financial information to the management, councillors and state authority on a monthly basis. For auditing purposes, they disclose financial information on a yearly basis. However, the MLAs are not required to disclose their financial information to the federal government unless requested to do so and it is not mandatory. In general, the MLAs are satisfied with the financial information they provided.

7.4 Data Content and Data Organization

Gibbins et al. (1992) refer to the data content as “the basic numbers or words disclosed…such as accounting figure (s), financial projection (s), capital offering characteristics, bonuses paid to senior officers, or technical characteristics of a new mine” (p.16). Managing data content may involve arranging business affairs that is beyond the accounting calculations or policy choices in order to produce desired disclosure content (Gibbins et al., 1990). Data organization is “a set of pigeonholes for data, existing in advance and waiting to be filled” (Gibbins et al., 1992, p. 18). It involves organizing, classifying and arranging information for presentation. In other words, it is concerned with where a figure appears in the financial statements because such placement is believed to be informative.

In general, the content and organization of financial statements of local councils do not differ much from the standard format of financial statements. As claimed by the Finance Director of Omega the council does prepare Balance Sheets, Income Statements, Statement of Changes in Reserves, Cash Flow Statements and the Notes to the Financial Statements. This is in line with the statements that are normally prepared by private entities:

Actually, the form and content of our financial statements does not differ much from the private entity’s financial statements. The full set of financial statements comprise of different sections. For example, the first section shows the audit certificate. Second section is the statement by the President and the councillor; basically by the councillor who has a tertiary education in accounting or professional accountant. This is followed by declaration of
principle officer responsible for financial management in council. The next pages present a normal full set of accounts which include The Balance Sheet, The Income Statement, The Statement of Changes in Reserves, The Cash Flow Statements and finally the Notes to the Financial Statements (AAO1).

The Finance Director of Omega further remarked that the difference could be found in the Notes to the Accounts:

The difference maybe in the Notes to the Accounts because we do have notes on the extra ordinary even such as landslides and other natural disasters full with their history. This maybe rarely found in the normal set of financial statements in the private sector (AJO1).

It is apparent from the interviews that there is no specific financial reporting requirement imposed on local council in preparing their financial statements. This problem is acknowledged by all the councils. For example the Assistant Finance Director working at Alpha claimed that this was the case at that particular council body:

As far as I am concerned, there is no specific financial reporting requirement imposed on local council in preparing our financial statements (KKA2).

This view was also expressed by the Director of the Internal Audit Unit of Beta and the Treasury Director of Delta.

The absence of accounting standards has given local authorities considerable discretion regarding the treatment of accounting items and their presentation and disclosure in the financial statements. This discretion has been characterized by differences in the content and format of annual financial accounts between the local authorities in Malaysia. As suggested by the Assistant Director of Treasury Department at Alpha:

All details in the financial statements are depending on the council itself to determine. The councils themselves decide what is suitable or appropriate to their practices (KLA2).

In the absence of specific reporting requirement, the interviews revealed that MLAs referred to Local Government Act 1976, Treasury Instructions, Treasury Circular,
Treasury Circular Letters, Financial Procedure Act 1957, Financial Reporting Standards, and State Authority Circular to guide the preparation and presentation of financial statements. This is illustrated by the comment from the Finance Director of Alpha:

Our main references are the Local Government Act 1976, Treasury Instructions, Treasury Circular (changes to Treasury Instructions) and Treasury Circular Letters (highlight details of circular) that is applicable to us. Treasury Instructions, Treasury Circular and Treasury Circular Letters are circulated by Ministry of Finance. We sometime refer to Financial Procedure Act 1957. We do use the Financial Reporting Standards by Malaysian Accounting Standard Board. However, we do not apply all of the standards. For the budget preparation, we use the Treasury Circular (KLA1).

However, consistent with Tayib et al. (1999) and Tooley et al. (2010), the Malaysian Government Treasury Instructions and Circular are given the highest priority by the accountants in MLAs as the main references for the preparation and presentation of the financial statements. For example, according to the Treasury Director of Delta:

In preparation of financial statements, in most of the local council, we make use of the Federal Treasury Instructions and Circular as the main references. We use these for the preparation and presentation of our financial statements (SLD1).

The above statement is supported by the Treasury Director of Beta who commented:

Our main reference is the Treasury Instructions and Treasury circular. We prepare our financial statements based on accruals basis (JJB1).

The interviews also revealed that The Local Government Act (1976) does not stipulate the required form and content of the financial statements. As stipulated in Section 53, The Act only required the local council to prepare and keep their financial statements. The Act does not provide any reference on the form, content and organization of financial statements. For example, the Assistant Finance Director of Alpha commented that the Act 171 only required the council to prepare financial statements:

We are required to prepare financial statements as stipulated in Section 53 of the Act 171. However, this Act does not state the details regarding the form and
content of financial statements. It just provides general information. That is why for the purpose of financial reporting and disclosure, we follow Treasury Instructions and Treasury Circular (KKA2).

The Act 171, however, leaves it to the state authority to determine the form and content of the financial statements. According to Section 54 (4), “Such annual statement shall be prepared in such form and shall contain such information as may be required by the State Authority”. However, consistent with Coombs and Tayib (1999), the interviews revealed that the state authorities have yet to issue any guideline on the form and content of financial statements. As illustrated by the comment from the Treasury Director of Alpha below:

The Act (171) does not state clearly the content and form of our financial statements. The Act leaves it to the State Authority to determine the form and content of our financial statements. However, there is still no specific standards or reporting requirements that have been issued by the state authority up to now (SSG1).

The interviews also revealed that the accountants in MLAs have maintained a good relationship with the Auditor who checks their financial statements. They admitted that they seek the Auditor’s advice when they are unsure on certain accounting transaction matters. This is revealed by the statement from the Director of Treasury Department of Alpha:

We have a good relationship with the Auditor General. I normally call or e-mail the Auditor General’s office regarding the presentation, content and format of financial statements and seek for their advice (KKA1).

The interviews also acknowledged the Auditor’s role in advising the local councils on the data content and organization of financial statements. However, advice and recommendations by the Auditor need to be tabled to the FAC meeting for approval before they can be applied. For example, the Assistant of Treasury Department of Delta acknowledged the important of the external auditor in advising them on the presentation of their financial accounts. She added that the auditor will update them with the latest accounting standards:
Most of the presentations of our financial accounts are advised by the auditor. If there is an update on accounting standards, the auditor will inform us and we need to bring this matters to the FAC meeting for approval before we can apply them (LLD2).

The financial accounts of all the local councils participating in the study are audited on behalf of AG by the difference private sector audit firms appointed by the state authority based on the recommendation of the AG. This means that each local council is audited by a different audit firm. They are normally appointed for the period of three years before the appointment of a new audit firm. Once the audit is completed, the private auditors then submit their audit findings and reports to the AG. As explained by the Finance Director of Alpha:

Our accounts are not directly audited by AG. Private audit firm who is appointed by the state authority based on the recommendation by the AG audits our accounts on their behalf….They are all very experienced auditors. Normally, the private auditors are appointed for the period of 3 years. Each local council is audited by different auditor…Once they (private audit firm) completed the audit, they will send the reports to AG. The AG then will communicate with us to discuss the issues related. The AG will make contact directly with us to discuss the findings of the appointed auditor (KKA1).

The interviews also revealed that the difference in local councils’ data content and organization of financial statements may be due to the advice given by different private auditors. According to the Treasury Director of Gamma.

For each local council, we are audited by difference audit firm. Furthermore, in one local council, for instance Gamma, the private auditor is replaced by different private auditor once their contract finished. Normally the auditor is appointed for a 3 year term. Therefore, we (MLAs) are having a problem because different auditor may have different opinions and advice..because we (MLAs) are advised by different auditor, each council may have different presentation in its financial statements (SSG1).

In summary, the interviewees claimed that the content and organization of financial statements of local councils do not differ much from the standard format of financial statements. The interviews revealed that there is no specific financial reporting requirement imposed on local council in preparing their financial statements. In the
absence of specific reporting requirement, the MLAs referred to several references. However, the FTC is given the highest priority by the accountants in MLAs as the main references for preparing their financial statements. The interviews also acknowledged the External Auditor’s role in advising the MLAs on the data content and organization of financial statements.

7.5 Reasons for Disclosing Financial Information

The reasons for disclosing financial information are presented in Table 7.3. The interviews revealed that the most mentioned reason for disclosure is because it is required by the legislation, mainly the Local Government Act 1976. Section 53 of this statute states: “The local authority shall cause proper books and accounts to be provided and true and regular records to be entered therein of all transactions of the local authority and such books and accounts shall be open at all reasonable times and for reasonable periods to the inspection of any Councillor with the prior consent of the Mayor or President”.

Table 7.3 Reasons for Disclosing Financial Information

<table>
<thead>
<tr>
<th>No.</th>
<th>Reason for Disclosing</th>
<th>Number of Interviewees (A total of 20 interviewees responded to the question)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Required by Legislation (Act 171)</td>
<td>15</td>
</tr>
<tr>
<td>2</td>
<td>Monitoring and Decision-making purposes</td>
<td>15</td>
</tr>
<tr>
<td>3</td>
<td>Auditing purposes</td>
<td>8</td>
</tr>
<tr>
<td>4</td>
<td>Financial assistance</td>
<td>6</td>
</tr>
<tr>
<td>5</td>
<td>Budget approval</td>
<td>6</td>
</tr>
<tr>
<td>6</td>
<td>Openness and transparency</td>
<td>5</td>
</tr>
<tr>
<td>7</td>
<td>Sharing the information</td>
<td>5</td>
</tr>
<tr>
<td>8</td>
<td>Feedback from the public</td>
<td>2</td>
</tr>
<tr>
<td>9</td>
<td>Change public mentality</td>
<td>2</td>
</tr>
<tr>
<td>10</td>
<td>Attract the higher level governments’ (federal and state) attention</td>
<td>2</td>
</tr>
</tbody>
</table>

For example, the Assistant Treasury Director of Beta commented that Act 171 required them to prepare the financial statements and the financial accounts need to be inspected by any councillor at any reasonable time. She added that Act 171 also required the
council’s financial statements to be audited by the AG or another auditor appointed by the state authority on the AG’s behalf:

We are obliged under Section 53 of Local Government Act 1976 to prepare the annual financial statements. Therefore, it is important for us to obey this regulation. The Act also states that the financial statements need to be inspected by any councillor at any responsible time or period. The Act also required that the financial statements need to be audited by the AG or other auditor appointed by the state authority based on the AG recommendation (JJB2).

In addition, Section 55 (5), for example, required the MLAs to forward their budgets to the state authority for approval, stating: “After the Budget has been passed by the local authority it shall be forwarded to the State Authority not later than the twentieth day of November and shall be considered by the State Authority not later than the thirty-first day of December of that year and the State Authority may reduce or reject any item of expenditure appearing therein”. This provision is explained by the Treasury Director of Alpha in her comment below. She explained that the council forwards the budget to the state authority for its approval. She further asserted that the council’s money can only be spent after the budget is approved by the state authority:

We forward budget to the state authority for approval as required by Act 171 under Section 55 (5)...The state authority then tables the budget in the State Legislative Assembly for approval. Once approved, the budget is gazette. We can only spend the money after our budget is approved by the state authority (KKA1).

The second most mentioned reason for financial disclosure is that of monitoring and decision-making. Financial disclosure to the management of the local council, the councillors and the state authority enables them to be informed of the council’s financial performance and position. The Treasury Director of Treasury of Alpha explained that the purpose of financial disclosure is to let the management and the councillors know the financial performance and financial position of the council. More frequent financial disclosure to the management and councillors enables the council to identify any problems at an early stage and execute strategies to overcome them:

The purpose of disclosure is to let the management and the councillors know our collections as compared to our budget. Same goes to spending as compared to our initial budget. Whatever we have budgeted, we must spend them. From this monthly disclosure, we are able to make sure whether our budget is
sufficient enough to meet the commitments until end of the year. Therefore, it is very helpful in our decision-making and internal control processes. The financial statements tell the story of our performance for the whole year. For example, decision such as whether we have sufficient fund to be spent in certain project or if we need extra fund and what should we do to achieve the collections target. So, these processes enable us to identify problems at an early stage and steps need to be taken to overcome the problems and take necessary remedial actions (KKA1).

As discussed earlier in this chapter, the MLAs also disclose their financial information to the state authority on a monthly basis. The interviews revealed that the financial disclosure to the state authority is for monitoring and decision-making purposes, as indicated by the Assistant Director of Beta. She further explained that by disclosing such financial information, the state authority is able to identify which council(s) is/are in a good financial position and which council(s) is/are struggling with their finances. The state authority may then take necessary action to help those councils that are struggling with budgetary difficulties:

The purpose of the disclosure is to keep the state authority informed of our financial performance and position. Once we disclose financial information to them, they will do the analysis and comparison. The purpose of the analysis is to know the financial position and performance of local councils. So, once they know our financial position and performance, it makes it easy for them to monitor us. They will be able to know which local councils perform better and which local councils need help. They will be able to know which local councils perform better in the collection and which local councils are struggling with it. The state authority has set a standard on the current assessment taxes collection. They have set up the standard that the collection must be 90% of total current assessment taxes. For the arrears, local council needs to collect more than 50% a year (JJB2).

The third reason for financial disclosure is for auditing purposes. Section 60 (1) of the Local Government Act 1976 states: “The Auditor General or other auditor appointed by the State Authority on the recommendation of the Auditor General shall, throughout the financial year, inspect and examine the accounts of the local authority, and the local authority shall, by the Treasurer or other officer authorized by the local authority, produce and lay before the auditor all books and accounts of the local authority together with all vouchers, papers, contracts and documents relating thereto”. With this in mind the Treasury Director of Gamma commented that the council’s financial accounts are audited by the private auditor on behalf of AG as required by Act 171. She added that it
is a normal practice for the AG to send a team to the councils having problems with their financial statements and conduct further auditing and suggest recommendations for improvement:

As required by Act 171, we are audited by the private auditor appointed by the state authority on behalf of AG. The private auditor send reports to AG once audit completed. Therefore, we disclose financial information to the Auditor General (AG) for the auditing purposes. Besides, the AG also interested to know the performance and the financial management of the local council. If they found out something wrong, they will come and make a query. This is true for the councils which received qualified or adverse report. The AG normally sends a team to investigate the financial statements of council which seems to be problematic. They will perform another audit and in the end they give recommendations for the improvement (SSG1).

The fourth reason why the local councils disclose financial information is for financial assistance reasons. Given the persistent deficits in some local councils in Malaysia, grants given by both the state and federal governments seem to be inevitable (Setapa, 2003). However, unlike federal to state grants which are constitutionally determined, both federal to local government and state to local government grants are not and the flow is not guaranteed and largely depends on discretion. For instance, the Treasury Directors of Gamma explained that the council discloses the financial information to the federal and state governments so that they are able to know the financial position and financial performance of each council. This information is used to determine which councils need financial help:

We received grant from both Federal and State Governments. In order to give us the grant, there are certain requirements. The Federal requirements may be different from State requirements. We normally apply for both grants from Federal and State Governments. Therefore, we disclose the financial information to them (Federal and State) so that they are able to know our financial position and performance. The financial information help them to make decision on how much the grant should be given to each council or on the decision whether or not council should be given a grant (SSG1).

Similarly, the Finance Director of Alpha explained that the council discloses the financial information to the state authority so that it knows about the financial position and performance of the council and how much assistance is needed:
State government is like our parents. Disclosure of financial information to the state authority means we want them to know our financial position and performance and we want them to know which councils are having financial difficulties. If we are having financial difficulties, we normally request a grant or other form of financial assistances from the State Government. If we want to request the grant, for example, development grant, they will consider our financial position and performance. If the financial position of the council is strong, normally no grant will be granted. If we have the financial difficulties, normally State Government will help us. That is why disclosure of the financial information to state authority is crucial (KLA1).

The fifth reason why local council discloses financial information is for budget approval. Local councils’ budgets in Malaysia need to be approved by their state authorities. This is stipulated in Section 55 (5) of the Local Government Act 1976: “After the Budget has been passed by the local authority it shall be forwarded to the State Authority not later than the twentieth day of November and shall be considered by the State Authority not later than the thirty-first day of December of that year and the State Authority may reduce or reject any item of expenditure appearing therein”. This reason is highlighted by several respondents. For example, the Finance Director of Gamma explained:

The purpose of financial disclosure is for budget approval purposes. As stated under section 55(5), our budget is approved by State Government (SSG1).

Reasons such as sharing information as well as openness and transparency are mainly raised by local councils that disclose their financial information on their websites. The Treasury Director of Beta expressed the need for her council to share information with the public because the council collects the money in the form of assessment taxes and other revenues. She further added that by such disclosure they are able to know how the council spends their money:

Local council is established to serve the public. We collect the assessment taxes from the public. Therefore, we need to get the public informed on how we spent their money. That is why our financial statements need to be audited to make sure that we manage the money appropriately (JJB1).

Similarly, the Finance Director of Omega commented that they disclose the financial information online because the council wants to share information with the public,
which will then be aware of what is happening in the council as well as in the area under its administration:

We disclose financial information because we want to share the information with the community. For example, in the case of natural disasters such as landslide …..although we don’t disclose all the costing due to lack of expertise, we still need to disclose the event because it has the impact on the value of the land in the area. In addition, the issues here are whether or not each of the residents in that area are entitled to claim from the insurance because they may not be aware of that (AAO1).

Some councils believed that there are benefits in being more open and transparent. This reason is linked to an expressed need to change the public’s mentality. For instance, the Director of Audit Unit of Beta commented that the council has been more open and transparent with its financial information since 2008. He further commented that there are some benefits of being more transparent with the financial information and providing it online. By sharing the financial information the public knows how the council spends the money and this may help to change the public’s opinion of the council. Furthermore, he believed that the more transparent the council is with financial information, the greater the public’s willingness to pay their taxes:

When we are more transparent to the public, especially the taxpayers, they will be able to see how we spend their money. In my opinion, being transparent is better. This may reduce the public’s perception of the council that we always misappropriate their money. I believe that the more transparent we are, the more they willing to pay for their taxes. That is why we do disclose our financial information in the website… We have published the financial information in our website since 2008. So, if the public, specifically the taxpayers would like to get the financial information, the can access them from our website (JJB4).

The above statement is supported by the comment made by the Treasury Director of Beta. She asserted that most of the council activities are financed by collections from the public. Therefore, there is a need for the council to share the financial information with the people. By sharing financial information, the public, especially the taxpayers, are able to see where the council spends their money. She added that this may overturn the public’s negative perception of the council:

We disclose financial information in the website for the purpose of being more transparent with the financial information. Our activities are financed by the
public money. We collect assessment taxes, licenses, compounds from the public. Our major revenues are assessment taxes. Therefore, we need to show them how we spend their money. For example, we spend their money for drainage system, road maintenance, building repairs and some other activities. For most of the people, they think that the collection of assessment taxes is for the use of waste management only. They failed to see some other works we do. This includes when natural disasters happen in the area under council’s administration. So, all of these works are paid by using our collections. Therefore, disclosing financial information may help reduce negative perception of the public on how we spend their money (JJB1).

The interviews also revealed that the purpose of financial disclosure is to obtain public feedback. For example, the Finance Director working at Omega commented on this strategy:

…by disclosing the information, we will be able to get good feedbacks and recommendations from the so called “professional” out there especially from the “elite” group who staying in the our area without having to pay for consultation fees (AAO1).

Finally, another reason for the financial disclosure is to attract the attention of the federal and state government. The Finance Director of Omega commented that her council may not only receive financial assistance, but also professional advice and other technical assistance:

…sometimes we disclose information, for example, the natural disaster events because we want to attract the attention of state and federal government. As a result, they will provide us not only with the financial assistance, but in term of professional advice and technical assistance as well (AAO1).

In summary, the interviews revealed that the main reasons for the disclosing of financial information in the MLAs are to meet the requirements of the Local Government Act 1976 and to monitor and make decisions on how monies are spent. Another reason given by the interviewees is for auditing and financial assistance purposes, budget approval, being more open and transparent, sharing information with the public, to obtain feedback from the public, to change the public’s view of local government and to attract federal and state government support.
7.6 Chapter Summary

This chapter analyses two broad research questions: firstly, how MLAs disclose their financial information; and secondly, why they disclose financial information. The interviews revealed that financial statements, budgets and monthly reports are the main mediums for the disclosure of financial information in MLAs. The interviews also revealed that other mediums of disclosure are annual reports, websites and speeches by the mayor/president of the local council. In addition, the interviewees revealed that the MLAs disclose the financial information internally and externally, and this varies in frequency from a monthly to a yearly basis. The interviews also revealed that most of the local councils are satisfied with the adequacy of the financial information they provide in their reports. The interviewees claimed that the data content and organization of the financial statements in MLAs do not differ much from the standard format of financial statements that are used in private sector organizations. However the interviews revealed that there is no specific reporting requirement imposed on MLAs with regards to the form and content of financial statements. Most MLAs refer to The Local Government Act (1976) and the Treasury Instructions and Treasury Circulars when preparing their financial statements.

As for the reasons why they disclose financial information, two main reasons emerged. They disclose the financial information because it is required by the Local Government Act 1976 and for the purpose of monitoring and decision-making. Another reason given by the interviewees concerns auditing and financial assistance, budget approval, being more open and transparent, sharing information with the public, obtaining feedback from the public, changing the public’s opinion of local councils and to attract the attention of federal and state authorities.
CHAPTER EIGHT

INTERNAL/EXTERNAL INFLUENCES AND EXTERNAL MEDIATOR(S)
THAT INFLUENCE FINANCIAL DISCLOSURE PRACTICES

8.0 Introduction

This chapter analyses interview evidence collected in the field and supported by the review of published sources in public records (newspapers and information provided on MLAs’ websites), annual reports, monthly management reports, legislative documents, financial reports, etc. with the intention of explaining the internal/external antecedents that influence financial disclosure decisions and how these influence such decisions. The interviews also aimed to identify external mediators that influence financial disclosure practices and explaining how they do so. This chapter is organized into three parts as follows. The first part introduces the chapter. The second part identifies and discusses the internal and external antecedents. The third part identifies the external mediator and explains how this variable influences financial disclosure decisions.

8.1 Antecedents of Disclosure

Gibbins et al. (1990) suggest that the disclosure position of the organization is understandable in terms of a set of internal and external antecedent conditions. This section identifies and explains the antecedents of disclosure of MLAs.

8.1.1 Internal Antecedents

Gibbins et al. (1990) identified three categories of internal antecedents that might influence an organization’s disclosure position: a firm’s history, corporate strategy and internal politics. Consistent with Gibbins et al. (1990), the interviews reveal that the most common factor that influences the disclosure practices in MLAs is a collective view from management of how disclosure should be practiced. Similarly, Adams (1997) also found evidence in reference to the influence of dominant personalities in the disclosure process. Gibbins et al. (1990) explain at length the importance of this factor by stating that:
…it was often clear that management’s attitude toward disclosure reflected CEO’s attitudes... Important disclosure decisions were described as group decision; e.g. an issue is discussed face-to-face or a disclosure is drafted and circulated for comment…Such process allow the disclosure position of the firm to emerge as a consensus or, where there are divergent opinions, as a compromise….The attitude of the CEO and the degree of internal consensus on disclosure issues thus affect the firm’s disclosure decision (p. 131).

In MLAs, executive powers lie with the mayors of city councils, and presidents in the municipal and district councils. The mayor or president are supported and/or overseen by a system of committees (Phang, 2008a). The mayor or president, as an administrative head of the local authority has substantial influence on how the local authority is to be run and he/she is answerable to the state government (Kuppusamy, 2008). The mayor or president is effectively the head of council, comprise of 8 to as many as 24 members appointed by the state government. He establishes a number of committees with selected councillors serving as a members, presides over council meetings, policy-making and other businesses (Haidar et al., 2004). Decisions are normally made at the committee level before brought forward to the full council meeting generally for endorsement (Kuppusamy, 2008). However, Section 10(7) states that if the Mayor or president does not agree with the other councillors on certain decisions, he/she can refer the matters to the Chief Minister or the ‘Menteri Besar’ of the state whose decision thereon final and binding on the local authority. Therefore, the provision provided in the Act 171 has given Mayor or President a substantial influence on how the local authority is to be run. This includes the financial management and disclosure practices of MLAs. As revealed by the interview findings in Chapter 6, as a “controlling officer” of the council, the Mayor/President is responsible for the local authority’s income and spending.

As revealed by the interview findings in Chapter 6, the disclosure decisions are made by the mayor/president of the local council and/or the FAC. It is a normal practice of the accountant in a local council to get approval from the mayor or president before they disclose any financial information. For example, the Finance Director of Alpha pointed out that he always get advice and approval from the council president before he discloses financial information to the FAC:
We in the finance department prepare the financial statement. We normally seek advice from the president if we believe that the disclosure of certain financial matters will tarnish the council’s reputation. The President is the “controlling officer” in term of the management of council. Hence, if we (The President and Finance Director) feel that the financial matters are appropriate to be disclosed, only then we bring them to FAC meeting. If they are not, I just then notify the President. It is the power of the president who is the “controlling Officer” of the council to make decision whether or not to disclose financial information (KKA1).

Thus, the interview evidence suggests that before the financial information is disclosed to other internal or external stakeholders, the Finance/Treasury Directors normally first bring them to the mayor/president for his/her view and advice. The interviews also revealed that some financial matters and financial disclosure issues are decided at the meeting.

The statement by Alpha’s Internal Auditor shows that the president influences disclosure issues especially with reference to budget decisions. She claimed that the president can override the decisions made by other councillors in the FAC:

There is a time where councillors are not agreed with our proposed budget. However, the President has an absolute power to override the councillors’ decision should he agreed with the proposed budget…This budget then later be disclosed to state authority for the approval. Therefore, his decision is crucial. He has a power to make decision even though the decision is made by him alone (KKA7).

Furthermore, the accountants are aware where the mayor/president stands on disclosure issues particularly when they are “sensitive”. The mayor or president’s perspective has been commented on by the Finance Director of Gamma:

The answer whether we want to disclose certain information is in the hands of the President especially when it is related to “hot and sensitive issues”. …our President is very cautious in disclosing any “sensitive” financial information (SSG1).

The interviews indicate there is evidence that the FAC’s views are affecting the way disclosure is practiced. In MLAs the mayor or president establishes a number of committees with selected councillors serving as members (Haidar et al., 2004). The
committees help the local government in management and decision-making. The number of committees depends on local governments’ plans including that for development (Setapa & Lin, 2003). Committees’ responsibility for approving financial policy and any changes to the policy are evident in the Treasury Director of Delta’s following comment:

We have a Finance and Assessment Committee that responsible for the council’s financial matters and policies…. This committee is responsible to discuss and decide on the financial issues and to approve financial policies (LLD1).

This view is reinforced by the Senior Accountant at Omega who revealed that the Finance and Assessment Committee is responsible for approving the accounting policy of the council based on the recommendations and advice from the accountants, especially advice coming from the Treasury Director:

Normally, anything related to financial matters need to be brought to the FAC meeting. The committee approves the accounting policy (s) based on the recommendation and advice from the accountants, particularly the advice from Treasury Director (AAO2).

A statement by the Treasury Director of Gamma revealed that the FAC reviews and decides on financial regulations, procedures and policies:

The Finance Committee meeting review and decide the financial regulations and procedures...This committee also assess and decide on financial policies (SSG1).

However, as the committee is chaired by the mayor/president, it is easy to obtain a consensus from the committee members on disclosure decision matters. For instance the Assistant Treasury Director of Delta revealed that most of the financial disclosure decisions are decided at FC meetings. She further claimed that the President as a chairperson of the FC and the council’s controlling officer may exercise his discretion regarding financial disclosure decision during these meetings:

I must say that most of the financial disclosure decisions are decided in the Finance Committee meeting. In other words, the matters are actually needed to be tabled, discussed and decided together in the Finance Committee meeting.
this meeting. The President as the chairman of the committee and as a Controlling Officer of the council can exercise his discretion (LLD2).

Similarly, the Finance Director of Beta revealed that, as long as they disclose the information in accordance with the established rules and procedures, the FAC normally agrees with the advice of the mayor and Finance Director:

We need first to get approval from the Mayor, who normally sits in the Finance Committee and chairs the committee, as well as the Finance Committee before we disclose any financial information. Most of the decision regarding the disclosure of financial information are decided in this committee….I must say that most of the time, based on the advice from the Mayor and/or Finance Director, the Finance Committee does not have much problem on what we want to disclose. They are very co-operative as long as we disclose them in line with the established rules and procedures (JJB1).

Therefore, the interview evidence suggest that the views of the mayor/president and the FAC on disclosure issues are important and thus affect on how financial disclosure are practiced.

Previous disclosure practices are also seen as an internal factor driving how disclosure is practiced in local councils. Gibbins et al. (1990) in fact emphasize that the organization’s history contributes to the formation of a disclosure decision. This can be contributed in two ways; first, “the firm’s traditions, taken-for-granted ways of doing things, may establish how disclosure is managed” (p. 130). Secondly, “people learn from rewards and penalties they receive, the disclosure consequences experienced by managers become the basis of beliefs about disclosure” (p. 130). Consistent with this, the firm’s history and previous practices have been mentioned by the interviewees as impacting on their disclosure position. The accountants learn from their past experiences in how to handle financial disclosure practices. For instance, the Finance Director of Delta explained that their practices are affected by the long-established rules and procedures:

Our annual financial reporting and disclosure are greatly influenced by previous practices. We just follow the established rules and procedures of the previous practices…. We disclose financial information as required by the regulation. What we disclose in the financial statements is a routine practices because what we disclose is more or less the same every year (LLD1).
This statement was backed up by the Finance Director of Alpha, who claims that they
normally disclose sufficient and stable levels of information in financial statements. She
adds that they have learned from previous experience in how to handle their financial
disclosure practices. As claimed by her, there are not many changes to the disclosure
practices of her council, except in terms of figures. She further claimed that if changes
happened, it is more on the Notes to the Accounts section and normally recommended
by the external auditor:

The reporting and disclosure practices are actually a “cut and paste” from the
previous practices. We learn from previous practices and actually there are not
many changes to the disclosure practices. The changes are merely on the
figures, not on the format or content of financial statements….We just follow
the standard procedures. Basically, we produce sufficient levels of information
in our financial statements….In addition, if there is a change, most of the
changes are on the notes to the accounts. These changes are normally advised
by the external auditor (KKA1).

Another internal influence on the disclosure practices of MLAs highlighted by the
interviewees is the number of accountants with the experience and expertise handle
financial management functions. As discussed in Chapter 6, their responsibilities are not
merely limited to financial management; they also advise the mayors and presidents and
FACs in making disclosure decisions. In fact, Adams (1997) found evidence that
supports a positive link between the number of accountants and financial disclosures.
He argues that the tendency to disclose more information and be more transparent in
corporate reporting is due to accountants’ professional training, peer pressure and legal
accounting standards and guidelines.

Given the position of advice to senior councillors in disclosure decisions, the experience
of accountants is crucial. For instance, the Finance Director of Alpha emphasizes the
importance of experience of the accountant:

Given the position to advise the President and FAC in making disclosure
decision, I would say experience and expertise are crucial. We have five
accountants in the council. Accountants know best when it comes to accounting
and finance matters in local council and we are the expert in this area. At the
same time, given the workload as an accountant in the local council, we must
adopt to the environment quickly. Even, if you do have the qualification, but
you failed to adapt to the environment, you might fail to work as an accountant
in the local council (KAA1).
Likewise, the experience of the mayor/president in handling disclosure issues is also considered to influence disclosure practices. Gibbins et al. (1990) emphasize the importance of experience in handling finance-related issues “because people learn from the rewards and penalties they receive, the disclosure consequences experienced by managers become the beliefs about the disclosure” (1990, p. 130). Past experience seems to be very important as a guide to a disclosure decision. For example, the Finance Director of Alpha described their council’s president as very experienced in disclosure practices and that he handles it professionally with advice from the accountants:

Our President is very experience in disclosure practices. He has been in the council years and he has been dealing with the disclosure practices for long time. He has the power to instruct us whether or not to disclose certain financial information…Although most of the times he needs our advice, he can handle disclosure issue professionally based on his experiences (KKA1).

The number of professionals in the FAC is also deemed to have an influence on the disclosure practices. For instance, the Finance Director at Delta contends that the different professional backgrounds of the councillors who sit on the FAC has influenced the council’s financial practices because they give different opinions and views on disclosure issues. At the FAC meeting, all opinions of committee members are taken into consideration as long as the opinions and views are in line with the rules and procedures. As indicated by this director’s comment below:

The committee members (FAC) are councillors. The committee is chaired by the President. Currently, the FAC members comprise of three professional accountants who work in the corporate sector; two businessmen with finance and business background; two lawyers; one former lecturer, one engineer, and the remaining are from NGOs (non-government organizations). They are from various professions. As their background is different, each of them has their own opinion on one particular issue. Therefore, we receive lot of different comments and recommendations during the meeting. For those councillors with the accounting knowledge, they do give comments and recommendations up to the technical level. I consider this is good because we will get different opinions and views for different professional backgrounds in financial matters and issues,…The Committee normally take their views into consideration as long as they are not against the rules and regulations (LLD1).

Council culture in dealing with information disclosure has also been mentioned by the interviewees as influencing disclosure practices. More than 30% of the interviewees and
all those working in municipal and district level of councils claimed that their councils are conservative and treat the financial information somewhat as private and confidential and that the information should not be disclosed to the public or any person not mentioned in the Local Government Act 1976. As there are no proper reporting requirements that have been imposed on the MLAs, they refer to the Federal Treasury Circular in their reluctance to disclose anything other than required by the circular. The Finance Director of Alpha implied this in his statement:

I have been in the council for a long time and I am aware that we are greatly influenced by our conservative culture. We have a great reluctance to disclose anything to anyone or any party that is not stated in the Act (Local Government Act 1976)…..Furthermore, we only disclose information in accordance to Federal Treasury Circular only…As I said earlier on, we don't even disclose financial information that we treat as "sensitive" information to the councillors (KKA1).

However, contrary to the above claimed, two larger councils claimed that they are more open in disclosing financial information. They claimed that their councils have the desire to become more transparent and that they publish financial information on their websites. They admitted that most of the resources used to pay for government operating activities are funded by various taxes and rates. By disclosing financial information, the public can see how the council employs public funds. At the same time, this might help to change the public’s negative perception of the council. This is illustrated by the statement from the Public Relations Officer of Beta:

Our council is becoming more transparent nowadays. This is better because when we are more open with the financial information, the public are able to see how we utilize their money. At the same time, this can change the public’s perception that we always misuse their money (JJB5).

In addition, these councils believed that being more transparent may change the public’s perceptions of local councils and be more willing to pay their taxes and rates. Furthermore, they believed that by being more transparent better feedback will result and suggestions from the public, especially professional groups. Such feedback and suggestions might help improve government services. For instance, the statement below by the Finance Director of Omega points to this theme:
Most of our activities are funded by assessment taxes and other funds from public…In my opinion, it is necessary for us to share the financial information with the public… By being more transparent in disclosing the financial information, we hope that the public will be more willing to pay for their taxes…By disclosing the financial information, they might be able to see that the local councils in Malaysia as not as rich as they thought. Furthermore, if we don’t have sufficient revenues, they know that they may not be able to enjoy good facilities and services…at the same time, by sharing and disclosing the information to the public, we will be able to get good feedbacks and recommendations from the so called “professional” out there especially from the “elite” group who currently staying in our area without having to pay for consultation fees (AAO1).

To sum up, the managements’ view on how disclosure should be practiced, previous disclosure practices and the number and experience of accountants all seem to have a significant internal influence on disclosure practices. In addition, a council’s culture and the desire to be more open to the public are also regarded as important influences on its disclosure practices.

8.1.2 External Antecedents

Gibbins et al. (1990) identified two categories of external antecedents that might explain a firm’s disclosure position, namely external institutional and market factors. Gibbins et al. (1990) state that “disclosure is affected by legislation, standards and regulations which apply to a firm contingent on laws under which the firm was chartered” (p. 131). This statement was supported by the interviews where basically the three main Acts - The Street, Drainage and Building Act 1974 (widely known in Malaysia as Act 133), the Local Government Act 1976 (Act 171), and the Town and Country Planning Act 1976 (Act 172) - help regulate MLAs’ operations. As explained by the Director of the Internal Audit Unit at Beta:

Basically, the councils operate based on their own Act, which is Local Government Act 1976 (Act 171). Besides, we do have several other laws such as The Street, Drainage and Building Act 1974 (Act 133); Town and Country Planning Act 1976 (Act 172) some other laws such as by-laws. These laws are created to help local council to run and operate their daily activities (JJB4).
The same Director explained that Act 171 is the most important instrument for accounting purposes as it outlines the general financial provisions of MLAs as and their requirement to keep proper records and books of account:

However, the general financial provisions are mainly explained by Act 171. This Act states that the local council must prepare their financial statements. However, the statement in the Act is very general. No detail requirement of the financial statements preparation and reporting are explained and mentioned in the act (JJB4).

Similarly, the Finance Director of Gamma stated that one of the reasons they disclose financial information is because it is required by the Act 171. Nevertheless, as asserted by Gibbins et al. (1992) “the precise form of financial disclosure is rarely spelled out in the regulations. There remains a great deal of uncertainty as to how disclosure should be prepared and the likely consequences, if any, of alternate disclosures” (p. 55). Likewise the interviews revealed that Act 171 does not offer specific details pertaining to form and content of financial statements:

The Act 171 does state the procedures such as when we suppose to disclose the financial information to the council, when we suppose to pass our budget to the state authority and that the financial information should be disclosed to councillors and all that… However, the statement in the Act is very general. No detail requirement of the financial statements preparation is mentioned in the Act (SSG1).

The Act 171 however, leaves it to the state authority to determine the form and content of MLAs’ financial statements. All accountants and Internal Auditors claimed that there is still no specific reporting requirements currently being issued and enforced by a state authority. As noted by the Finance Director of Beta:

The Act leaves it to the state authority to determine the form and content of our financial statements. However, there are still no specific standards or reporting requirements that have been issued by the state up to now (JJB1).

The absence of specific financial reporting requirements has compelled the accountants of MLAs to refer to other sources for preparing their financial accounts and reporting processes. The accountants in MLAs refer to several sources such as Financial Procedure Act 1957, the FTC, the circulars issued by the state authority, the circulars
issued by Ministry of Housing and Local Government and the Financial Reporting Standards set by the Malaysian Accounting Standard Board (MASB) for readying their financial accounts, budgets and annual reports. For example the Finance Director of Alpha listed the sources he uses:

In preparing of the budget, financial statements and annual report, we do refer to FRS by MASB. Besides that, we do refer to Financial Procedure Act 1957, Treasury Instructions and Treasury Circular (changes to Treasury Instructions) that is applicable to us. We also use the State Circular and Ministry of Housing and Local Government. However, those Circular are more on work procedures… Out of these, most of the time we refer to Federal Treasury Circular (KKA1).

All the Finance Directors and accountants interviewed conceded that FTC is the main reference for preparing financial accounts. The Finance Directors of Beta, for example, provided support for these claims:

For the presentation, form and content of financial statements, most of the time, we refer to Federal Treasury Circular…In local council, for some of the revenues and expenses, we use accruals basis. For this reason, we normally refer to FRS (Financial Reporting Standards) by Malaysian Accounting Standard Board. Therefore, I would say that, we mainly refer and adopt Treasury Circular and we modify them to suit to our financial disclosure environment…Sometimes we refer to FRS (JJB1).

Although the guidelines advised by FTC have received the greatest priority by the accountants of MLAs to prepare their financial accounts, the adoption of FTC is voluntary rather than mandatory. For example, the Finance Director of Delta explained that not all guidelines applied to them, claiming that some of the guidelines are not suitable to local council accounting practices:

However, there is no statutory or non-statutory provision stating that we should adopt the FTC in preparing the financial reports and accounts. Therefore, we don’t apply FTC in full. Some are not applicable to us. The process is, we self selected the guidelines by FTC and supposed we want to apply or use them, we do the proper proposal and bring them to the Finance Committee Meeting and Full Council Meeting for approval and endorsement. If approved, then only we can use them. Therefore, it is selective. We choose methods that are applicable to us only. We have no choice because we don’t have any proper or specific financial reporting requirements. We hope that we have AP specifically for local council (LLD1).
The evidence collected from the interviews revealed that one of the reasons why FTC has received the greatest priority from the accountants in MLAs is because they are audited by the AG who normally makes extensive use of guidelines. According to the Finance Director of Beta:

Like Federal Government and State Government, we are all dealing with public money. Therefore, the AG has the right to comment and advice on our financial statements as they are the one who audit our financial statements. In auditing our financial statements, the AG mainly refers to the Treasury Circular (JJB1).

Similarly, the interview evidence claimed that by complying with FTC requirements, the MLAs have shown proper stewardship of public monies and also demonstrated their ability to manage affairs and resources efficiently and effectively. As commented on by the Director of the Audit Unit at Beta:

I have a lot of experiences in auditing the government statutory bodies. The FTC is used by all federal and state government including government statutory bodies. Therefore, the adoption and compliance of FTC in MLAs mean we are in line with all other governments, which means we have maintained a proper accounts on public monies and able to show a proper stewardship of public monies. Furthermore, it also able to demonstrate our ability to manage affairs and resources efficiently and effectively in achieving their policies (JJB4).

Therefore, the adoption of the Federal Treasury Circular has influenced the disclosure practices in MLAs.

Disclosure practices at the MLAs were also influenced by the disclosure practices of other councils. The interviews indicated that the accountants working in these MLAs have maintained a good relationship with each other. They normally refer to accountants from other councils when unsure about how to disclose certain accounting items. They also consult them if they are not sure how to implement new circulars. This is evidently the case in smaller councils which often refer to either the same level or larger councils when uncertainty arises. According to the Finance Director of Gamma:

Having the difficulties from the absence of the specific reporting requirements and standards, we normally follow the practices of other local councils. If I am unsure of certain accounting treatments, or unsure about new circular, I normally refer to the accountants from other local councils….We maintain a close relationship with other accountants from other councils….I must admit that the fellow accountants from other councils have helped us a lot. Most of
the time, I refer to the fellow accountants at the same level. I even have a
discussion and guidance from the accountants from larger council (SSG1).

Furthermore, they conceded that they will copy the practices of other councils
especially those that have implemented new practices successfully. It is normal practice
for MLAs’ accountants to discuss disclosure practices with accountants from other
councils. For instance, Assistant Finance Director of Alpha said:

I would say other councils’ disclosure practices do influence our financial
disclosure practices. For example, if we have newly created expenses or
revenues, we need to find a way to disclose these new expenses or revenues. In
this case, we will refer to other councils who have experienced and been
through this process and have disclosed this kind of expenses or revenues in the
financial statements….Normally, we follow their successful practices. It is a
normal practice that we meet and call other accountants from other councils
and have a discussion on the financial disclosure practices. I think every
accountant in Selangor does this (KKA3).

In summary, the regulations and accounting guidelines and procedures, particularly the
adoption of the Federal Treasury Circular do influence disclosure practices in MLAs.
These influences are particularly in terms of presentation of financial statements, form
and content of the financial accounts and reporting of financial information. The
absence of specific financial reporting requirements has compelled the accountants to
refer to other sources, especially the FTC when readying their financial accounts and
reporting functions. It is evident that the adoption of FTC is voluntary and not
mandatory. Finally, the disclosure practices of other councils were suggested by the
interviewees as influencing disclosure practices in MLAs.

8.2 Influence of External Mediators

Gibbins et al. (1990) described external advisors as the individuals who help “identify
disclosure issues and related norms and opportunities” (p. 132). They acknowledge
several roles of external advisors such as assisting in identifying financial issues,
helping in identifying the specific formal or informal rules associated with a particular
disclosure, providing technical advice and an opinion which effectively shifts some risk
of the decision away from management and their involvement adds credibility to
disclosures. The external advisors may also be used as a strategic resource in bargaining
situations where alternative interpretations of events are possible (p. 133).

In the current study, all accountants and internal auditors interviewed acknowledge the
roles of the AG and appointed private auditors as external advisors in their financial
disclosure practices and decision-making. Generally, the credibility and assurance of
financial information presented in the financial report of MLAs is made possible
through auditing (Healy & Palepu, 2001). Here the responsibility to provide such an
assurance lies with the AG. All accounts of MLAs need to be audited by the AG as
stipulated in Sec. 60 of the Local Government Act 1976 (Act 171). Sec. 60 (1) of Act
171 notes: “The Auditor General or other auditor appointed by the State Authority on
the recommendation of the Auditor General shall, throughout the financial year, inspect
and examine the accounts of the local authority, and the local authority shall, by the
Treasurer or other officer authorized by the local authority, produce and lay before the
auditor all books and accounts of the local authority together with all vouchers, papers,
contracts and documents relating thereto”.

Nevertheless, all the councils’ interviewees claimed that their financial statements are
not directly audited by the AG. Each local council is audited by a private auditor who is
appointed by the state authority based on the recommendation of the AG. The private
auditor is normally appointed for a period of three years. As explained by Finance
Director of Alpha:

Our accounts are not directly audited by the AG. Private audit firm who is
appointed by the State Authority based on the recommendation by the AG
audits our accounts on their behalf….They are all very experienced auditor.
Normally, the private auditors are appointed for the period of 3 years. Each
local council is audited by different auditor… Their opinions are
different…once they completed the audit, they send the reports to AG. The AG
then will communicate with us to discuss the issues related. The AG will make
a contact directly with us to discuss the findings of the appointed auditor
(KKA1).

Once the audit process is completed the external private auditors then report the
findings directly to the AG. An audit certificate will then be issued to the local
authorities following this. The processes are the same for all the councils as explained
by the Finance Director of Beta:
We need to complete our full set of accounts by March every year. Then, by April, we need to present them in the Financial and Assessment Committee Meeting for approval. Once approved, the financial statements then are presented in the Full Council Meeting for endorsement. For this purpose, The Full Council Meeting is held before 30 April every year. Once approved, the financial statements then are signed by Mayor/President, one councillor and Treasurer. Once endorsed, we send the draft financial statement to the AG for the auditing purposes. Then we receive the response from the AG. Once we received the confirmation, the audit process begins. The process takes 2 to 3 weeks. The longest is about two months. The private external auditors then report the findings to the AG. We then have an exit conference with the AG and the private external auditor. After the exit conference, the AG issues the audit certificate. Once the certificate is issued, that means the financial statements is audited and finalized. The financial statements then be gazette and we can publish the financial statements in the website (JJB1).

In this study, all the accountants interviewed emphasized the important influence of external auditors on their financial disclosure and practices. These findings are consistent with Gordon et al. (2002), Adams (1997) and Giroux (1989). These influences are more evident particularly in the presentation, form and content of the financial statements. As explained by Finance Director of Alpha:

The Auditor General plays important roles on our financial disclosure especially on the preparation of financial statements. They advise us especially on the disclosure of items in the financial statements….Basically, we prepare our financial statements according to Federal Treasury Circular and the Act (Act 171). The AG roles are to make sure whether or not we prepare our financial statements according to these regulations. Therefore, I must say that the form and content of our financial statements is guided by the circulars and advice from the AG (KKA1).

His statement is further supported by the Assistant Finance Director of Delta. She explained that most of the presentation in financial statements is advised on by the external auditor. She further claimed that the FTC does list the minimum reporting requirements but details on the presentation and format of financial statements are not explained by the FTC:

Most of the formats are advised by them….Content of the financial statements is basically based on our activities. Most of the presentations are advised by the audit….The Treasury Circular does list the minimum statutory reporting requirement…However, the circular (Treasury Circular) does not explain in detail the format as well as the form and content of financial statements...
Therefore, I must admit that most of the presentations of our financial accounts are advised by the external auditors (LLD2).

The accountants interviewed also conceded that they normally have a good relationship with the external auditor and the AG. They do make personal contact with the external auditors in order to seek advice if they are unsure about certain financial issues. As stated by the Finance Director of Omega:

We do maintain a good relationship with the AG and appointed external auditor. We received a lot of advice from external auditor and AG on the preparation of financial statements. We do call them if we have any queries…I normally e-mail the external auditor and AG regarding the presentation, content and format of financial statements and seek for their advice. Besides that, we have an exit conference with AG. In the conference, we normally seek advice from them on the preparation of our financial statements especially its form and content (AAO1).

According to the accountants interviewed, they normally follow the advice and suggestions of external auditors. For instance, the Finance Director at Omega claimed that they accepted more than 90% of suggestions and recommendations made by the external auditors. This signifies that such advice and recommendations does influence the presentation of financial statements and their form and content:

I must say that the AG and appointed external auditor are playing a significant role in the financial disclosure practices of local council….I understand that the main concern of the AG is to make sure that the financial statements is prepared according to acceptable rules and regulations and that financial statements is prepared in “true and fair” manners… I must admit that the external auditors including AG have given us a lot of advice and recommendations for improvement especially in the presentation and content of our financial statements….I must say that we accept and follow ninety to ninety five percent of these recommendations. The reason why we don’t follow hundred percent simply because the recommendations are not approved by the FAC or President as they feel that the recommended practices are not suitable to be applied to our council (AAO1).

The Finance Director of Beta provided an example of the recommendations given by the external auditors. She claimed that they prepare and present the statement of equity in their financial statements because it is required by the AG:
Before this, we did not have the equity statement. We started to prepare the equity statement in 2008. We prepare the equity statement because it is a recommendation and requirement by the AG. The AG advised us to prepare the equity statement. We just follow the AG’s requirement (JJB1).

The Finance Director of Beta explained that one of the reasons they always seek for the external auditor’s advice is because their council wants to improve the quality of its financial statements. She added that the aim for a clean audit certificate explains why they always get in touch with the external auditor. She further noted that a clean audit certificate is important for the council as it may affect people’s confidence in the council’s ability to manage public funds:

The way we present our financial statements is similar with the previous practices. In order to improve the presentation of financial statements, we normally ask the opinion from external auditor. We always want to improve the quality of our financial statements so that our financial information is presentable, readable and understandable to others. We always refer to external auditor to make sure that we are preparing the right thing. Even before we prepare the yearly financial statements, we normally refer to external auditor….They normally give us comments and recommendations on how to improve them…At the same time, we always hope that we receive a clean audit certificate. It is important because it affects the public confidence on the capability of how we manage their fund. Therefore, as the audit certificate is issued by the AG, it is important for us to prepare financial statements as required. Therefore, we need their (external auditor) advice (JJB1).

The interviewees especially the accountants acknowledge that the external auditors update them when new reporting policies and practices are introduced. When a new circular has been published, they normally seek a clarification and an explanation from the external auditor:

I must say that the feedback, input and recommendation from the auditor are very important. When there is new standard or circular, we normally seek advice from the external auditors…They normally the one who highlight the disclosure issue (s) before we can bring them to the FAC meeting (LLD1).

The audits, both Auditor General and Appointed Private Auditor play significant roles in advising us with the policies and format of our financial statements. They are the one who normally recommended new practices and policies for our financial statements preparation and financial reporting purposes (LLD2).
The accountants also seek advice from the external auditors when there is conflict among circulars they have received. As illustrated by the Finance Director of Alpha:

We sometimes encounter a conflict between circulars. For example, according to circular from the Secretary of the Ministry of housing and Local Government, we need to submit the financial statements for auditing not later than 1 June, but the circular from the Treasury (Federal Treasury) says that the financial statements must be submitted for auditing not later than 30 April. Therefore, there is a conflict here. We sought advice from AG and it recommended that we should follow the Treasury Circular….Similarly, when there is a new circular; we normally seek advice from AG whether or not we should apply them (KKA1).

Consequently, the Assistant Finance Director of Delta claimed that a change in the accounting policy is normally advised by the external auditor. Similarly, external auditors advise MLAs on the way items which are not included in the treasury circular should be disclosed:

Normally, a change in the accounting policy and accounting treatment is based on the advice from the appointed external private auditor and Auditor General…. Most of the accounting treatments that are not to be found in the treasury circular are advised by the Auditor. For example, the treatments for accrual revenue and expenses (LLD2).

In addition, the accountants of MLAs conceded that the external auditors normally keep them update with the new accounting standards and circular. For instance, the Finance Director of Delta admitted that he normally receives an update of the new standards or a circular during the audit “exit conference”. When he is unsure about certain standards he normally seeks advice from the external auditor:

In preparation of financial statements, in most of the local council, we use Federal Treasury Instruction (AP) and approved accounting standards (FRS) that are applicable to the local council. We use these as a reference for the preparation our financial statements. Normally, we are updated with the new standards during the audit….The external auditor normally update us with the new standards….I would have to say that the external auditors as a main source of our reference…..They are the only source we have pertaining to the updated standards. They are the one who always updating us. They normally notify us with any change in the accounting standards during the audit “exit conference….. I have to admit that, sometimes, we are unsure whether to use or not some new standards or circular. That is why we need advice from external auditor (LLD1).
The interviewees also revealed that there might be a slight difference in term of the form and presentation of financial statements, as and the term used for an account name in financial statements. For example, according to the Finance Director of Alpha:

For example, for balance sheet, some local council use the term “kunci kira-kira” and some local council use the term “lembaran imbangan” …we are using the term “kunci kira-kira” for balance sheet (KKA1).

The Treasury Director at Omega revealed that the difference in the financial statements between MLAs could be in terms of the details in the financial statements and how the Notes to the Accounts section has been designed:

If you look at to other councils’ financial statements, the format is actually almost the same. The difference maybe in term of the details they put in the financial statements and how they design the notes to the accounts. Some council prefers their financial statements as detail as possible. Some design them simple. Some of the local council put many notes to the accounts and some prefers few notes. Notes to the accounts are depending on the preference of each local council. There is no standard format for the wording, content and their form (AAO1).

Another difference is indicated by the Finance Director of Beta, who explained that some local councils maintain the stock account while some local councils do not:

For example, in Beta, we maintain a stock account for medicines, stationeries, fuel (petrol and diesel), spare parts etc….. In some local council, they do not have a stock account. So, this kind of differences that I am talking about (JJB1).

The interviews revealed that the differences in form and presentation of financial statements may be due to varied advice from different external auditors. This seemed to be the case according to the Finance Director of Beta:

We receive different advice and comments from different private external auditors. This means, different private auditor preferred different presentation of financial statements. Each council is audited of different private auditor. Therefore, one of the reasons for the differences is due to different opinion by different private auditor who audits the local council. I must say that, our financial statements are normally presented based on the audit comments and
recommendations. That’s why you may see a slight difference in financial statements presentation among local councils. However, I must say it just a slight difference. Most of the financial statements are similar (JJB1).

Even in the same council any difference in the presentation of the financial statements could happen if the council is audited by different audit firms over time. As suggested by the Finance Director Alpha:

As I said earlier on, that is why you will see the presentation of our accounts might be different from other councils because we are audited by different audit firms. For example, our previous auditor advised us to separate our Non-Current Assets. Previously we separate Non-Current Assets and Work-in Progress Accounts with different notes to the accounts. However, with the current auditor, they advise us to combine the accounts (KKA1).

Although the accountants of MLAs routinely seek and concede that they generally follow the advice of their external auditors, the decision whether to accept or not to accept the advice and recommendation is still in the hands of the mayor/president and/or the FAC. The accountant cannot simply apply any accounting policy without having approval first. This was confirmed by the Assistant Director of Delta:

I would say that the external auditors have an influence on our disclosure practices especially in the form and content of our financial statements. However, I must say that, the council (the Major and/or Finance Committee) may accept or reject any suggestion from external auditors including AG as the decision is actually in the hands of council itself. Any change in the policy as a result from the External Auditor advice need to be tabled in Finance Committee Meeting and be treated as new accounting policy. Any policy needs to be approved. Only approved policies can be applied. However, we don’t simply apply the recommendations by the External Auditors. It depends on the suitability and relevancy. Furthermore, any change on policy and procedure is subject to the councillors’ (Finance Committee) and President’s approval (LLD2).

In fact, it is a normal situation in the local council whereby the opinion of the councillors or president is not in favor of the external auditor’s advice and recommendations. The Finance Director of Delta explained that when this happens, the decision of the president or councillors in the committee prevails is governed by Act 171:

It is normal when sometimes the decision of the President or councillors in the Finance Committee meeting might not be in the favor of what the external
When this situation happens, we need to follow “the legal standing”. Meaning we need to refer to the Act 171. The council has the right to accept or reject the recommendation by the external auditor. If the auditors question why we don’t follow their recommendation, we need explain to them the President or councillors rejected their recommendations and to show them the minutes of the meeting (LLD1).

Therefore, the external auditors can be regarded as the external mediator because accountants in MLAs frequently seek advice from external auditors particularly in the disclosure issues. Accountants tend to generally follow the recommendations of external auditors and this is confirmed by Gibbins et al. (1990).

In summary, the interviews revealed that legislation, standards and regulations such as the Local Government Act 1976, the FTC and accounting standards are all regarded as important external influences on the disclosure practices. These documents are regarded as the sources for preparing the financial statements, budgets as and annual reports, particularly in term of their presentation, form and content. The interviews further revealed that the typical local council in Malaysia sometimes copies the disclosure practices of other councils especially in the case of successful disclosure practices. The accountants of MLAs admitted that they generally have a good relationship with other councils’ accountants and the external auditors and that they are always discuss disclosure practices. Table 8.1 below summarizes the important internal, external influences and external mediator on the disclosure practices of MLAs.

**Table 8.1 Important Influences on Disclosure**

<table>
<thead>
<tr>
<th>Internal Influences</th>
<th>Number of Interviewees</th>
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<tbody>
<tr>
<td>A collective management view of how disclosure should be practiced</td>
<td>19</td>
</tr>
<tr>
<td>Historical antecedents, for example previous practices</td>
<td>16</td>
</tr>
<tr>
<td>Number and experience of professional, for example experience of accountant</td>
<td>11</td>
</tr>
<tr>
<td>Council’s culture</td>
<td>5</td>
</tr>
<tr>
<td>Desire of the council to becoming more transparent</td>
<td>5</td>
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<table>
<thead>
<tr>
<th>External Influences</th>
<th></th>
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<tbody>
<tr>
<td>Federal Treasury Circular &amp; Accounting Standards</td>
<td>16</td>
</tr>
<tr>
<td>Regulation – Local Government Act 1976</td>
<td>13</td>
</tr>
<tr>
<td>The disclosure practices of other councils</td>
<td>8</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>External Mediator</th>
<th></th>
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<tbody>
<tr>
<td>The advice and views of external auditors</td>
<td>17</td>
</tr>
</tbody>
</table>
8.3 Chapter Summary

This chapter analyzed and explained two broad research questions: What are the internal/external antecedents which influence financial disclosure decision and how do these antecedents influence such decisions? How do external mediators influence financial disclosure decisions? The chapter reveals that managements’ view on how disclosure should be practiced, their previous disclosure practices and number and experience of accountants hired all seem to have a significant internal influence on disclosure practices. In addition, a council’s culture and the desire to be more open to the public are also regarded as impacting on a local council’s disclosure practices.

Legislation, standards and regulations such as Local Government Act 1976, the FTC and accounting standards are all regarded as important external influences on the disclosure practices of MLAs. The chapter also reveals that the councils in Malaysia sometimes copies the disclosure practices of other councils. The accountants of MLAs admitted that they generally have a good relationship with other accountants from other councils and that they regularly discuss disclosure practices.

Finally, this chapter indicates that the accountants of MLAs routinely seek and generally follow advice from the external auditors, who are regarded as the best source pertaining to disclosure issues. They concede that the external auditors update them with the latest standards and circular of financial reporting. The best possible explanation for the differences in the presentation as well as form and content of their financial statements is due to the different advice from different external auditors.
CHAPTER NINE

DISCUSSION AND CONCLUSION

9.0 Introduction

This chapter discusses the findings using theory and the existing literature. The chapter begins with a summary of the main findings including discussions on financial disclosure decision-maker(s), the identification of stakeholders and medium of disclosure and a summary of reasons for disclosing financial information. This is followed by discussions on the organizational and environmental factors that influence the disclosure position and practices in MLAs. The chapter also explains the key contributions of this research in terms of theory and methodology and makes practical recommendations for policy and future research. Finally the limitations of this thesis are acknowledged.

9.1 Internal Structure Handling Financial Disclosure

The importance of the internal structure in managing financial disclosure has been emphasized by Gibbins et al. (1990). The authors argue that there will be more disclosure activity for a given issue or given disclosure position if certain structures are in place. Further, Gibbins et al. (1992) argue that the presence of particular specialists in an organization can shape the manner in which issues are identified and resolved. Therefore, from an organizational perspective, the presence of specialist subunits with responsibility for disclosure matters determines whether and how the organization will attend to and manage disclosure activities.

The interview evidence revealed that financial management is generally the responsibility of the Treasury/Finance Department in MLAs. This responsibility covers all collections, expenditures, payments, budget and accountings. This department is also responsible for updating all accounting records and preparing monthly, quarterly and annual financial standing reports and financial statements. In the case of financial disclosure decisions, the interviews revealed that the Director of Finance/Treasury Department normally does not make financial disclosure decisions. They do not have the authority to do so on their own. They may recommend and advise the
mayor/president and/or the FAC. In fact the interviews suggested that the accountants, particularly the Finance/Treasury Director, can only advise and recommend disclosure issues during the management and Finance and Assessment Committee meetings.

The interviews provide evidence that the disclosure decisions are normally authorized at the highest level within the local council, which is consistent with Gibbins et al. (1992). Gibbins et al. (1992) provided evidence that significant disclosures and changes in accounting policy are approved by a committee consisting of senior officers. Similarly, a study by Holland and Stoner (1996) of 27 large UK companies also claimed that voluntary corporate disclosure of price-sensitive information is authorized at the highest corporate level.

The interview evidence revealed that the mayor/president as the executive head of the local authority played significant roles in financial disclosure decisions and these findings are consistent with Kuppusamy (2008), Phang (2008a) and Haidar et al. (2004). As the administrative head, he/she has been given the authority to make financial disclosure decisions. Furthermore, the interview evidence reveals that as “controlling officer” of the council, the mayor/president is responsible for the local authority’s income and spending and answerable to the state government. The interview evidence revealed that it is crucial for the accountant in local council to get approval from the mayor/president before they disclose any financial information either internally or externally. This finding suggests that the mayor/president is the first person who needs to know the disclosure issues before they are disclosed to other stakeholders. Further, the interview evidence revealed that the involvement of the Mayor/President in the financial disclosure decision seems to be more crucial when the issues are associated with political and sensitive issues. However, the nature of the political and sensitive issues is not clear as the interviewees were reluctant to discuss them in detail.

Besides the mayor/president, the interview evidence also revealed that the FAC is responsible for making financial disclosure decisions. Consistent with Kuppusamy (2008), this suggests that the disclosure decisions are also made at the committee level. Majority of the interviewees claimed that the accountants, particularly the Finance/Treasury Director working at MLAs normally table the financial disclosure issues in the FAC meeting. The financial issues are then discussed and approved by the FAC members. Similarly, the financial policies of the council are also normally discussed and approved at the committee level. Consistent with Haidar et al. (2004), the
interview evidence revealed that the FAC is given the authority to approve the accounting policy and any change in the accounting policy in MLAs. However, the mayor/president as a chairman of the FAC and the controlling officer of the council may exercise his discretion on financial disclosure decisions during the FAC meeting. This discretion is particularly important when the FAC meeting fails to reach a consensus on certain financial disclosure issues or when there is a 50-50 split votes. In this situation, the mayor/president will use the voting system to his or her discretion. Furthermore, Section 10 (7) of the Act 171 provides that if the mayor/president does not agree with the other councillors on certain decisions, he/she can refer them to the Chief Minister or the ‘Menteri Besar’ of the state whose decision is final and binding. As for the quorum, the FAC meeting is valid only if it is attended by 3/4 of the FAC members. All financial disclosure decisions are later brought to the full council meeting for endorsement purposes. However, in practice, most councillors will not challenge the decisions that have been made in the committee level (Kuppusamy, 2008). Although it seems that financial disclosure involves more than one individual/committee in deciding what is to be disclosed, the interview evidence suggested that as the FAC is chaired by the mayor/president, it is easy to get consensus from the committee members on disclosure decision issues. For the five local councils interviewed, all the FACs are chaired by the mayor/president of the council.

To sum up, the interview evidence supported Gibbins et al.’s (1990) theorization on the importance of the internal structure in handling financial disclosure. From the organizational perspective, it is the presence of specialist subunits (Finance/Treasury Department) with responsibility as an advisor and the presence of the mayor/president and the FAC with the responsibility to make financial disclosure decision that determine whether the organization will attend to and manage disclosure activities. The interview evidence revealed that the Finance/Treasury Director and accountants have the capacity to advise and recommend to the mayor/president and the FAC during the management meeting and FAC meeting on disclosure issues. They however do not have the authority to make disclosure on their own. The interview evidence revealed that the authority is given to the mayor/president and FAC of the council.
9.2 Medium of Financial Disclosure

Regardless of whether operating in the private or public sector, financial information is essential for informed decision-making. Previous studies (e.g. Atamian & Ganguli, 1991; Mack & Ryan, 2006; Pilcher & Dean, 2009) have classified users of financial information in the public sector into internal and external stakeholders. In the case of MLAs, the interviews revealed that local councils normally disclose financial information to internal stakeholders such as managers and councillors, and to external stakeholders like the state authority, auditor and the Ministry of Housing and Local Government. The financial information disclosure to the mayor/president, councillors, the state authority and the Auditor are required by Act 171. However, the interviews revealed that the disclosure to the MHLG is voluntary rather than mandatory and only if requested by the federal ministry.

Regarding public disclosure, although the study by Tayib et al. (1999) revealed the desire of the taxpayers in MLAs that local government financial information be made available or disclosed to the public, this study revealed that there is no direct financial disclosure to the public just yet in the MLAs disclosure practices, with the exception of websites disclosure. Only two of the five councils interviewed are more open with their financial information and they have published their financial information on their websites. Medium of disclosure, data content and organization, and frequency of disclosure are three disclosure outputs that the organization attempt to manage according to Gibbins et al. (1990). With regards to the medium of disclosure in MLAs, there are six mediums/channels of disclosure mentioned by the interviewees. Out of these, the financial statements, budgets and monthly reports are identified as the main medium for the financial information disclosure in MLAs. Consistent with previous studies (e.g. Mignot & Dolley, 2000; Alijarde, 1997; Jones et al., 1985), these mediums are perceived by the interviewees as useful tools for monitoring and decision-making purposes.

Other mediums of disclosure identified by the interviewees include annual report, websites and speeches. Although annual reports which includes both financial and non-financial information disclosure have been argued by several researchers (e.g. Ryan, Stanley & Nelson, 2002; Kloot & Martin, 2001) as one of the main documents available for local authorities to communicate financial information about their activities to
stakeholders, the interview evidence in this study suggested that the annual report is not the main medium of disclosure in MLAs. This evidence is consistent with Mack and Ryan (2007) and Hassan, Hassan and Nor (2007). Interview evidence revealed that not all MLAs prepare the annual report since it is not mandatory. Instead it is prepared by MLAs which can afford it in terms of money and staff.

As discussed above, the website has not been used extensively as a medium for financial disclosure as financial disclosure via website is totally voluntary in MLAs. Website disclosure is only practiced by councils which have sufficient information technology facilities and adequate specialized staff who are employed to maintain the websites (Ghani and Said, 2010). Finally, the interview evidence also revealed that financial disclosure is done through speeches, hence the speech and budget speech by the mayor/president of the council is normally done in the full council meeting.

The data content and data organization of financial statements of MLAs according to interview evidence do not differ much from the standard format of financial statements. However, the interview evidence revealed that there is no specific financial reporting requirement imposed on local councils in preparing their financial statements. In the absence of specific reporting requirements, the MLAs referred to several sources of authority. However, the FTC is given the highest priority by the accountants in MLAs as the main sources of authority for preparing their financial statements. Further, it is acknowledged that the external auditors have played significant roles in advising the accountants working at MLAs on the data content and organization of its financial statements.

With regards to frequency of reporting, the MLAs as evidenced by the interview disclose financial information to the management, councillors and state authority on a monthly basis. As for auditing purposes, they disclose financial information on a yearly basis. However, financial information disclosure to the federal government is not mandatory. In general, the MLAs are satisfied with the financial information they provided.
9.3 Reasons for Disclosing Financial Information

Several reasons were identified by the interviewees as to why the council discloses financial information. Requirements by the legislation and for the purpose of monitoring and decision-making were mentioned by most of the interviewees. This signifies that the council is obliged by the Local Government Act 1976 to prepare the financial statement and to disclose the financial information to certain parties. For monitoring and decision-making purposes, the interviews suggested that financial disclosure to the management, the councilors, and the state authority enable them to be informed of the financial performance and financial position of the council. More frequent financial disclosure to the management and councillors enables the council to identify any problems at the early stage and execute strategies to overcome them. Hence, these findings are consistent with Lee (2008), Tooley et al. (2010b) and Mack and Ryan (2007) that the financial information is used for decision-making and monitoring purposes. Further, monthly disclosure to the state authority suggested that the information is used for decision-making and comparative purposes in order to determine which councils are financially and not financially sustainable. The state authority may then take necessary action to help those councils that are struggling with budgetary difficulties. This interview evidence is consistent with Pilcher and Dean (2009). Disclosure to the state authority can also be linked to another reason for disclosure revealed by the interviewees. This reason is for the financial assistance purposes. The persistent deficits in some of the local councils in Malaysia have required them to seek financial assistance in terms of grants and contributions from both the state and federal governments. However, both federal-local government and state-local government grants are not guaranteed of assistance and largely depended on the discretion of federal and state governments. As a consequent, each of local council interviewed received different amount of grant and contribution.

Councils also disclosed financial information in order to improve transparency. Some of the interviewees indicated that a council engages in website disclosure because it would like to improve its transparency. These councils believed that there are some benefits of being more open and transparent. For example, by disclosing financial information, the public is aware of what is happening in the council as well as in the area under its administration. Further, financial disclosure enables the public to know how the council spent their money which may help to change the public’s bad perception on council.
Several other perceived benefits such as enable the council to get the feedbacks from the public and some believed that the more transparent the council with the financial information, the more public’s willingness to pay for their assessment taxes. Thus, due to these perceived benefits, two out of five local councils interviewed have disclosed the financial information on their websites.

Several other reasons mentioned by the interviewees include for the auditing purposes, for budget approval, and to attract the higher level governments’ (Federal and State) attention.

9.4 Disclosure Position – Ritualism and Opportunism

The disclosure position of an organization has been identified by Gibbins et al. (1990) as consisting two dimensions: ritualism and opportunism. Gibbins et al. (1990) defined ritualism “as a propensity toward uncritical adherence to prescribed norms for the measurement and disclosure of financial information” (p.130). The ritualistic dimension implies a passive adherence to perceived disclosure norms by using routinized, bureaucratized procedures. Ritualistic behaviour is repetitive and the role of managers in the disclosure is passive. Thus, according to Gibbins et al. (1990) and Adams (1997), ritualism is synonymous with internal antecedent conditions such as a company’s history reporting practices and the company culture. It is also synonymous with external antecedent conditions on voluntary disclosure, such as industry norms of behavior.

Opportunism refers to a manager’s “propensity to seek firm-specific advantage in the disclosure or nondisclosure of financial information” (Gibbins et al., 1990: p.130). Thus, it involves an active role for managers in which disclosure is seen as opportunities to gain specific advantages by managing the disclosure process. Opportunism is synonymous with both internal antecedent conditions such as corporate strategy and the political motives of individual managers in the firm, and external influences such as signaling to investors, and consumers and industry regulators in order to achieve a competitive advantage (Gibbins et al., 1990; Adams, 1997). Thus, Gibbins et al. (1990) embrace both organizational and environmental (economic and institutional) influences on disclosure position or strategy. The next section discusses the interview evidence collected in the field on organizational influences and disclosure positions of MLAs.
9.4.1 Organizational Influences and Disclosure Position

Several studies such as Gibbins et al. (1990), Adams (1997) and Haniffa and Cooke (2002) acknowledge the importance of opportunism in corporate politics and the influence of the dominant personalities may have in the disclosure decision of the organization. The interview evidence gathered in this study provides support for this view. Indeed, majority of the interviewees reported that the attitude of the mayor/president on disclosure issues and a collective management view on how disclosure should be practiced is a major determinant of council’s disclosure practice. For example, the interview evidence suggests that before the financial information are disclosed to other internal or external stakeholders, the financial issues are normally first brought to the mayor/president for his/her view and advice. The interview evidence also suggested that the view of mayor/president is even more crucial when it comes to the disclosure of “sensitive” information. The mayor/president is an administrative head and holds executive power in MLAs. Interview evidence further suggested that, as a “controlling officer” of the council, he/she is responsible for the local authority’s income and spending and answerable to the state government. Therefore, he/she has been given the authority to make financial disclosure decisions.

Further, the interview evidence revealed that the views from the FAC also affect the way disclosure is practiced in local councils. The interview evidence revealed that for the purpose of financial management and decision-making, the council established the FAC. Thus, as suggested by the interview evidence, the financial disclosure decisions are normally made at this committee level and this committee is normally chaired by the mayor or president. The interview evidence also revealed that this committee is generally responsible for discussing and assessing financial issues, making financial disclosure decisions as well as approving financial policy and any changes to the policy. Therefore, the views of the mayor/president and the FAC could have a significant impact on their disclosure position.

Furthermore, the desire of the council to become more transparent was also reported to be important motives underlying more financial information disclosed publicly which could affect the medium of disclosure in MLAs. The evidence is provided by two councils (Beta and Omega). Several perceived benefits motivated these councils to becoming more transparent with the financial information. The councils perceived that
by being transparent, they are able to provide a clear picture of their situation that enables the public to see how the council utilizes their funds. Consequently, they claimed that this might help to change the public’s negative perception towards the council and the council may be benefited by getting more feedbacks and suggestions from the public especially from the professional groups. These feedbacks and suggestions are perceived by the councils to help them in improving their services. Therefore, the views of the mayor/president and the FAC as well as the desire of the council to becoming more transparent are considered to be an opportunistic phenomenon similar to that described by Gibbins et al. (1990).

Council previous disclosure practices and council culture regarding financial disclosure were also reported by several interviewees as internal factors driving how disclosure is practiced in local councils. Gibbins et al. (1990) emphasized that the organization’s history or disclosure practices contributes to the formation of a disclosure decision. According to them, this can be contributed through the firm’s traditions, taken-for-granted ways of doing things and through managers’ experiences and beliefs about disclosure. The interview evidence revealed that the disclosure practices in MLAs are very much influenced by previous financial disclosure practices. Further, the interview evidence suggested that disclosure practices of the council are frequently defined and determined by established rules and procedures and the council tended to produce fairly stable levels of information in their financial statements. Hence, this finding is consistent with Holland (2005) who claimed that previous practices become drivers of subsequent disclosure in the organization.

The interview evidence from three councils (Alpha, Delta and Gamma) suggested that council conservative culture has influenced the disclosure practices in MLAs. The interview evidence revealed that the councils treat the financial information somewhat as private and confidential. The councils are reluctant to disclose the information to the public or any person that has not been mentioned in the Act (Local Government Act 1976). A study by Adams (1997) also found that the company culture is a major determinant of organization’s disclosure practices. Therefore, the influence of previous practices and conservative culture on the disclosure practices of MLAs can be considered as a ritualistic phenomenon as described by Gibbins et al. (1990).

The number of professionals (e.g. accountants) hired to handle the financial management functions is another internal influence on the disclosure practices of MLAs.
suggested by the interviewees. As discussed earlier, the responsibilities of the accountants in local councils are not merely limited to financial management, but they are also given the position of advising the mayor/president and the FAC in making disclosure decisions. Therefore, the number of accountants hired in MLAs has an influence on the disclosure practices. A study by Adams (1997) found evidence that supports a positive linkage between the proportion of accountants and financial disclosure practices.

The experience of the mayor/president in handling disclosure issue is also suggested by the interviewees to have an influence on disclosure practices in the local council. According to the interview evidence, the mayor/president of the councils are very experienced in disclosure practices and he/she can handle the disclosure issue professionally with the advice from the accountants. The interview evidence further revealed that all the mayors/presidents have been working in the council for the period of not less than five years. All of them had served and been working in government sector with various previous positions for a long period of time. Therefore, according to the interview evidence, they are all well experienced in the public sector financial issues.

Moreover, the number of professionals in the FAC was reported by several interviewees to have an influence on the disclosure practices of local council. The interview evidence revealed that the councillors who sit in the FAC come from different professionals such as lawyer, accountant, lecturer, businessman and some are from non-government organizations. As such, the council receives different views and opinions from the committee members. All opinions and view are taken into consideration as each member in the committee has the right to give their opinion and view on each financial issue. Therefore, according to the interview evidence, the experience and number of professionals who have been given the authority to deal with financial issues have an influence on the disclosure practices in MLAs. Gibbins et al. (1990) indeed argued that “people learn from rewards and penalties they receive, the disclosure consequences experienced by managers become the basis of beliefs about disclosure” (p.130). Thus, as described by Gibbins et al. (1990), the number of professionals and their experiences in dealing with the disclosure issues is considered as ritualistic phenomenon.

In summary, while this study confirms the effect of internal antecedent conditions such as the internal politics and the organization’s history, the study did not find evidence on
the corporate strategy as suggested by Gibbins et al. (1990). The possible explanation for this might be due to the fact of the nature of the public sector and company strategy might be more appropriate for the free and open market competition scenarios (Feroz and Carpenter, 2001).

9.4.2 Environmental Influences and Disclosure Position

External institutional and market factors are identified by Gibbins et al. (1990) as two categories of environmental influences that might explain the firm’s disclosure position. With regards to external institutional factors, they stated that “disclosure is affected by legislation, standards and regulations which apply to a firm contingent on laws under which the firm was chartered” (p.131). The interview evidence gathered in this study provides support for this statement. The evidence also provide further support for Adams (1997) and Holland and Stoner (1996), who found that the regulations and standards are determinants of the disclosure practices.

In this study, the interview evidence suggested that Act 171 is the most important instrument for accounting purposes in MLAs as it outlines the general financial accounting requirements of MLAs as well as the requirement for MLAs to keep proper records and books of account. Further, most interviewees strongly suggested that one of the reasons for the council to disclose financial information is because it is the requirement of the Act 171. Nevertheless, as revealed by the interview evidence, the Act 171 does not stipulate any detail pertaining to specific form and content of financial statements. The Act 171 however leaves it to the state authority to determine the form and content of the MLAs financial statements in which there is still no specific reporting requirements currently being issued and enforced by the state authority as revealed by all accountants and internal auditors. The absence of specific financial reporting requirements has compelled the accountants of MLAs to refer to other sources such as Financial Procedure Act 1957, the FTC, the circulars issued by the state authority, the circular issued by MHLG and the Financial Reporting Standards set by the Malaysian Accounting Standard Board (MASB) for the preparation of their financial accounts, budget and annual report.
However, all accountants and auditors interviewed agreed that FTC is accorded the highest regard as a reference for the preparation of MLAs’ financial accounts. The adoption of FTC is nevertheless voluntary. There are no provisions in any instructions (statutory or non-statutory) stating that MLAs should adopt FTC in preparing their financial reports. One reason suggested by the interviewees as to why FTC has received the greatest priority from the accountants in MLAs in the preparation of their financial accounts and their reporting purposes is because they are audited by AG who normally makes extensive use of guidelines advised by FTC. Therefore, the adoption of the FTC could affect the nature and level of information contained in the financial reports of MLAs, particularly in the presentation, form and content of the financial reports. The voluntary adoption of FTC is interpreted as being an opportunistic phenomenon of the disclosure practices in MLAs as described by Gibbins et al. (1990).

The interview evidence also suggested that disclosure practices at the MLAs were also influenced by the disclosure practices of other councils. The interviews evidence revealed that the accountants working in these MLAs have maintained a good relationship with each other. The interviewees conceded that they will copy the practices of other councils especially those councils that implemented new practices successfully. It is a normal practice for the accountants working in MLAs to discuss the disclosure practices with accountants from other councils. Thus, the process by which accountants in MLAs routinely seek the advice and have a discussion with other accountants in other council on disclosure matters is considered to be a common ritualistic phenomenon as described by Gibbins et al. (1990).

This study also identified external auditors as another important influence on the disclosure practices of the MLAs. Gibbins et al. (1990) state that “disclosure opportunities are perceptual, not objective” and also “ritualism is activated by the perceived presence of external norms” (p.132). In this study, all accountants and internal auditors interviewed emphasized the roles of the AG and appointed private auditors in their financial disclosure practices. Gibbins et al. (1990) identified this role as external advisors and described them as individuals who help identify disclosure issues and related norms and opportunities (p.132). They acknowledge several roles of external advisors such as assistance in identifying issues, and are used to identify the specific formal or informal rules associated with a particular disclosure. External auditors also provide technical advice and an opinion which effectively shifts some risk
of the decision away from management. Further, their involvement adds credibility to disclosures. Such findings are also consistent with those reported in other empirical disclosure studies (e.g. Gordon et al., 2002; Adams, 1997; Giroux, 1989). The interview evidence collected in this study indicates that among other things, the external auditors provide advice to the accountants with regard to clarification and interpretation of accounting rules, update them with new reporting policies, accounting standards and circulars, advise them when there is conflict among circulars they have received and advise them with the presentation, form and content of their financial statements. The interview evidence also revealed that the accountant normally follow the advice and suggestions from the external auditors.

As each council is audited by different private external auditors on behalf of the AG, the interview evidence suggested that the difference in the form and presentation of financial statements could be due to different advice from different external auditors who audited their financial statements. Further, the interview evidence revealed that the reasons why they always seek for external auditor advice are because their council wanted to improve the quality of their financial statements and that the council aims for a clean audit certificate. In addition, the credibility and assurance of financial information presented in the financial report of MLAs is made possible through auditing. Thus, the responsibility to provide such an assurance lies with the AG. In this regard, the process by which accountants in MLAs, routinely seek and generally follow the advice of external auditors is considered to be a common ritualistic phenomenon (Gibbins et al., 1990; Adams, 1997).

In summary, consistent with Gibbins et al. (1990), the interviews revealed that legislation, standards and regulations such as Local Government Act 1976, the FTC and accounting standards are all regarded as important external influences on the disclosure practices of MLAs. These documents are regarded as the sources of reference for the preparation of the financial statements, the budget as well as the annual report of MLAs, particularly in term of the nature and level of information contained in the financial reports. The disclosure practices at the MLAs were also influenced by the disclosure practices of other councils. In addition, all accountants and internal auditors interviewed acknowledge the roles of the AG and appointed private auditors as external advisors in their financial disclosure practices and decision-making. The accountants working in these MLAs routinely seek and generally follow advice from the external auditors so as
to get a favourable audit report. However, the study did not find evidence on market factors as suggested by Gibbins et al. (1990). Possible explanation for this might be due to the fact that the MLAs are not engage in any product or capital markets.

9.4.3 Organizational and Environmental Influences of Disclosure Practice in MLAs

Consistent with Adams (1997), the empirical evidence in this study suggests that disclosure in MLAs is a complex phenomenon which is influenced both by organizational antecedent conditions and environmental antecedent conditions. Organizational influences such as a collective management view of how disclosure should be practiced, previous practices, council culture, number of professionals and the desire of the council to become more transparent have been suggested by the interview evidence to have an influence on the disclosure practices in MLAs. Similarly, environmental influences such as legislation, standards and regulations, and disclosure practice of other councils have been reported by the interview evidence to affect the nature and level of information in the financial reports of MLAs. The influence of external auditors is another important influence on the disclosure practices of the MLAs identified from the interview evidence.

The interpretation in this research is drawn from the model of disclosure suggested by Gibbins et al. (1990). There are strong similarities in term of the structures identified and the components of voluntary disclosure in both pieces of research. While this study confirms the effect of internal antecedent conditions such as the internal politics and the organization’s history, and environmental antecedent conditions, such as the legislation, standards and regulations, as well as the existence of external mediator (external auditor), this study did not find evidence on the corporate strategy and market factors. The possible explanations for this might be due to the fact of the nature of the public sector and the fact that the MLAs are not engage in any product or capital markets. Therefore, these factors might be more appropriate for the free and open market competition scenarios. Interestingly, unlike Gibbins et al. (1990), this study found that internal antecedent conditions such the desire of the council to becoming more transparent and organizational antecedent condition such as the disclosure practices of other councils as a significant influence to the disclosure practices of the MLAs.
Therefore, my results are in line with Gibbins et al. (1990) predictions. The results of the study suggest that the case councils’ readiness to disclose was a function of its developed disclosure position, the existence of internal structure for handling disclosure and the presence of external mediator (Auditors). Disclosure position has a number of significant internal and external antecedents. The difference between the studies may be attributed to the difference in the study setting. This study is conducted in the public sector environment (Malaysian Local Council) whereas Gibbins et al. (1990) sample was more widely disbursed comprised of both public and private regulated and unregulated firms. In addition, while Gibbins et al. (1990) study was conducted in a developed country, this study was conducted in a developing country.

9.5 Contributions of the Study

The study contributes to the disclosure literature through developments in theory and methodology, and through practical contributions.

9.5.1 Theoretical Contributions

The interpretation in this research is drawn from the model developed by Gibbins et al. (1990). This model discusses both organizational and environmental influences on disclosure strategy and thus it overcomes the consistent failure of the previous disclosure studies in taking into account organizational and environmental factors (Adams, 1997; Hopwood, 2000; Carpenter & Feroz, 2001). To the best of my knowledge, this is the first time that this model is used to explain the disclosure management and practices in the public sector, specifically at the local government level. This study suggests that this model is very useful for interpreting of case studies data. While this study confirms the effect of internal antecedent conditions such as internal politics and an organization’s history, and environmental antecedent conditions, such as legislation, standards and regulations, and existence of external mediator (external auditor), this study did not find evidence for a corporate strategy and market factors. This may be due to the nature of the public sector and the fact that the MLAs do not engage in any product or capital markets. Therefore, this study suggests that this model could be useful in explaining the disclosure practices in the public sector.
Moreover, the research findings of this study contribute to the literature in the area of financial disclosure, especially for emerging economies like Malaysia, by providing a greater understanding of disclosure management and disclosure practices. In particular, the findings of this study provide further evidence on who in the organization makes financial disclosure decisions, the range of issues considered when making disclosure decisions, the role of auditors and other external parties in the disclosure process, and the impact of external disclosure rules on disclosure decisions. These issues have not been explained extensively in other studies. As stated earlier, most studies on disclosure especially at the local government level have been done in Western or developed economies. This study, therefore, contributes to the literature by extending the scope of enquiry to an emerging economy, Malaysia.

**9.5.2 Methodological Contributions**

This study provides a methodological contribution by employing case studies at the local government level where only limited studies have been conducted. Thus, this research serves as a response to calls from several scholars (e.g. Kaplan, 1984, 1986; Palepu, 1987; McKinnon, 1988; Scapens, 1990; Merchant & Van der Stede, 2006) for the use of field study in explaining the disclosure practices of the organization. This field-based research utilized in-depth, semi-structured interviews involving participants such as directors or heads of Finance/Treasury Department, assistant directors, accountants, valuation officers, assistant accountants, internal auditor and public relations officer. Such intensive interviews from various participants who have direct experience in financial practices provide an informed and holistic view of the disclosure management and practices in MLAs, particularly factors that influenced the disclosure practices where there has been very limited research. These rigorous case studies in five MLAs have provided significant insight into explaining their disclosure management and practices. Thus, the findings of this study suggest that case studies research could contribute valuable insights into the complex and multi-dimensional phenomenon of disclosure and usefully complement conventional statistical analyses.
9.5.3 Practical Contributions – Policy Implications and Recommendations

9.5.3.1 State Authority, Ministry of Housing and Local Government and Professional Accounting Bodies

The Act 171 required the MLAs to prepare and report financial information. However, the interview evidence revealed that the Act 171 does not stipulate any detail pertaining to specific form and content of financial report and what consists of proper practice in compiling or keeping the record for. Although Local Government Act 1976 has given the authority to the state authority to determine the form and content of financial reports of MLAs, the findings revealed that there is no specific reporting requirement imposed in MLAs with regards to the form and content of financial statements just yet. The absence of specific financial reporting requirements has compelled the accountants of MLAs to refer to other sources for the preparation of their financial accounts and for the financial information disclosure purposes. For example, in the absence of the specific reporting requirement, the interview evidence revealed that MLAs have used FTC and other councils’ practices as the reference for preparation of MLAs’ financial accounts. Further, in the absence of the specific reporting standard the accountants of MLAs routinely seek and generally follow advice from the external auditors. Local government has been stated under List II of the Federal Constitution as a state matter. Therefore, it is about time for the state authority, as a regulator to issue the specific requirement statutory guidance to ensure the financial reports in MLAs to be more standardized and hopefully will be able to increase the credibility and quality of financial reports in MLAs.

Further, the findings of this study also reveal the lack of involvement of certain professional bodies in the development of MLAs financial disclosure methods. Professional bodies such as the Malaysian Institute of Accountants (MIA) and Malaysian Association of Certified Public Accountants (MACPA) according to some interviewees have expressed no or little interest in the development of MLAs’ financial disclosure. They have not made any significant contributions to financial disclosure practices in MLAs. Therefore, it is suggested the local government, state government and federal government through the Ministry of Housing and Local Government closely collaborate with these professional accounting bodies to further improve public sector financial disclosure at the local government level.
The empirical evidence here suggests that disclosure in MLAs is influenced both by organizational antecedent conditions, such as a collective management view of how disclosure should be practiced, previous practices, council culture, number of professional and desire of a local council to becoming more transparent, and environmental antecedent conditions, such as legislation, standards and regulations, and disclosure practices of other councils. Therefore, the regulators and legislators, especially state authority and accounting standard setters, may wish to take cognisance of these factors in developing external rules and regulations concerning financial disclosure.

9.5.3.2 Local Authority

The findings of this study revealed that two large councils are more open in disclosing their financial information and have published their financial information online. By disclosing the financial information, the public will be able to see how the council utilizes public funds. Further, by being more transparent, it may be able to change the public’s negative opinions of local councils and people are more willing to pay their taxes and rates. By being more transparent, the councils may get more feedback and suggestions from the public and this feedback may help to improve local government services. Other councils should be encouraged to publish their financial information on their websites because there are definite accountability benefits.

The interview findings suggested that local councils in MLAs refer to and copy the disclosure practices of other councils, especially larger and better resourced council. The absence of specific financial reporting requirements has compelled the accountants of MLAs to refer to other sources for the preparation of their financial accounts and for the financial information disclosure purposes, including other councils’ practices. The interview evidence suggests that the council will copy the practices of other councils especially those councils that have implemented the new practices successfully. When facing fundamental uncertainty about what action is appropriate and likely lead to success, an organization may select structures or practices which are used by other organizations which they regard as being successful in the institutional environment. A great deal of uncertainty as to how disclosure should be prepared could encourage the financial disclosures to be modeled on the behaviours of certain reference groups. Thus,
MLAs would learn a lot from other councils’ experiences, especially the successful ones which, in turn, could indirectly improve the disclosure practices in their councils.

9.6 Limitations and Future Research

Although this study has provided some useful theoretical, methodological and practical contributions, like any research it is not without limitations. Firstly, the findings of this study are constrained by focusing only on five councils and also restricted by a relatively short data collection period (four months). A more complete and comprehensive analysis of organizational and environmental factors is needed. In order words, a longitudinal study may be appropriate in order to further explain the disclosure management and practices in these organizations. This may expand the scope of future study to consider other aspects such as an emphasis on specific disclosure events or specific disclosure issues rather than general disclosure issues.

Secondly, like other field studies that rely on the interview as the main source data collection, this study suffers from problems of data credibility. Although people being interviewed had absolute freedom to express their views and their identity are fully confidential, it is possible that they might provide information that is favourable to the council. This in turn could result in subjective findings that might not reflect the true description of phenomena being studied. However, this study was performed using the triangulation approach in collecting data (documentation and interview), and for this reason any misleading information has been minimized. Furthermore, the current study conducted in-depth, semi-structured interviews with mostly accountants, and internal auditors, who although having much experience in financial management, do not have the authority to make disclosure decisions. Future investigations should include those responsible for disclosure decisions such as the mayor/president and councillors who are responsible for such policies. In this respect, a clearer picture will be obtained on local council disclosure management and practices.

Thirdly, the study can be extended to other government agencies to determine the consistency (or otherwise) in findings related to the disclosure management and practices and factors that influenced the practices. The future study could be conducted via a survey, interviews or the combination of both methods.
9.7 Concluding Remarks

The primary purpose of this study was to understand and explain the financial disclosure practices and disclosure management in MLAs. Applying Gibbins et al. (1990) model, the study sought to investigate who in the organization makes financial disclosure decisions, the range of issues considered when making disclosure decisions, the role of external mediators in the disclosure process, and the impact of external disclosure rules on disclosure decisions. Four research questions were used to explain: (1) How decisions regarding disclosure are made? (2) How does the organization disclose financial information and why does it disclose financial information? (3) What internal/external antecedents influence financial disclosure decisions and how do they influence financial disclosure decisions? (4) What external mediator influences financial disclosure decisions and how does it influence financial disclosure decisions? Based on these research questions, the conclusions of this research are thus.

Firstly, the research concludes that financial disclosure is authorized at the higher level within the council. Secondly, MLAs disclose financial information internally (to management, and councillors) and externally (to state authority, auditor and Ministry of Housing and Local Government). Medium for disclosure includes financial statements, budget and monthly reports, annual report, websites and speeches. Interestingly, there was evidence that the MLAs government are more transparent with the financial information and that they publish the financial information in their websites due to some perceived benefits. There are two main reasons for disclosure: to fulfill the requirement of the Local Government Act 1976 and for the monitoring and decision-making purposes. Another reasons are for auditing purposes, for financial assistance purposes, budget approval, being more open and transparent, to share the information with public, to obtain feedback from the public, to change public perception and to attract higher levels of government (Federal and State) attention.

Thirdly, the results of the study suggest that the case councils’ readiness to disclose financial information was associated with its developed disclosure position, the existence of an internal structure for handling disclosure and the presence of an external mediator. Disclosure position is influenced by significant organizational and environmental antecedent conditions. Therefore, this study concludes that the disclosure in MLAs is a complex phenomenon which is influenced both by organizational
antecedent conditions, such as a collective management view of how disclosure should be practiced, previous practices, council culture, number of professionals and the desire of the council to become more transparent, and environmental antecedent conditions, such as legislation, standards and regulations, and disclosure practice of other councils. Finally, this research concludes that external auditors play a significant role in disclosure practices in MLAs.

This thesis enhanced understanding of the disclosure management and practice in MLAs. The findings of this study have contributed to the existing literature by providing greater understanding of the disclosure management and practice in the public sector, particularly at the Malaysian local government setting. It also makes a contribution in terms of methodology in that the study suggested that case studies research could contribute insights into the complex and multi-dimensional phenomenon of disclosure and usefully compliment conventional statistical analysis.

The findings of this study may prove useful to a number of key groups in Malaysia, particularly State Authority, Ministry of Housing and Local Government, Professional Accounting Bodies and MLAs themselves.
Dear Datuk/Dato’/Sir,

INVITATION TO PARTICIPATE IN A PHD CASE STUDY.

I am pleased to invite you to participate in my PhD study entitled "ANTECEDENTS AND FACTORS INFLUENCING DISCLOSURE: A CASE STUDY OF MALAYSIAN LOCAL AUTHORITY".

I am a Tutor from Universiti Putra Malaysia (UPM), Bintulu Campus currently undertaking PhD studies in accounting at La Trobe University, Australia under a Malaysian Government scholarship. The PhD is being supervised by Professor Kamran Ahmed and Dr Robert Nyamori.

My PhD aims to understand the financial disclosure practices and disclosure management in Malaysian Local authority. Specifically, the study seeks to investigate who in the organization make financial disclosure decisions, the range of issues considered when making disclosure decisions (e.g. company culture, historical precedent and tradition, internal financial regulation, dominant personalities and professional groups), the role of consultants, auditors and other external parties in the disclosure process, the impact of external disclosure rules on disclosure decisions and to understand and explain why local authorities differ in the way they disclose financial information.
The study would involve a series of interviews with you, the top managers in all your departments and key people in in the finance department. The interviews would last between 30 minutes to one hour. During the study, I would participate in meetings as an observer and review documents relevant to decisions regarding financial disclosure. I would like to schedule interviews for May to July 2010.

All information provided will be treated with confidentiality and used strictly for academic purposes. No particular local authority will be disclosed individually nor would the names of the participants. The data from the study would be kept under lock and key at all times.

This study is potentially useful to you and the country in a number of ways. Firstly, through your participation, your organization will gain a better understanding of the issues surrounding financial disclosure. This understanding would be useful in directing local managers’ efforts towards perceived deficiencies in reporting. Secondly, the study would help regulators and policy making bodies to specify the form and content of accounting and reporting by local government councils. Lastly, the study would help other local authorities whose annual reporting might be inadequate.

I would be grateful if you could agree to participate in the study and look forward to receiving your letter of authorization.

Yours sincerely,

[Signature]

Neilson Teruki
PhD Candidate
School of Accounting
Appendix 5.2: Field-Site Interview Guide

Field-Site Interview Guide
Panduan Temubual Lapangan

Date(s) interview: __________________________
Tarikh temubual

I. Demographic Details
Name of Local Authority (LA): _______________________________________
Nama Pihak Berkuasa Tempatan (PBT)
Type of Local Authority: _______________________________________________
Jenis PBT
Name: ______________________________________________________________
Nama
Position: ______________________________________________________________
Jawatan
Number of years in current position: _______________________________________
Tempoh dalam jawatan sekarang
Number of years in Local Authority: _______________________________________
Tempoh berkhidmat dalam PBT
Other positions in the last 5 years: _______________________________________
Jawatan lain dalam 5 tahun terakhir _______________________________________
________________________________________

II. Managers Role in Financial Information Disclosure (Peranan Pengurus Dalam Pendedahan Maklumat Kewangan)
1. Briefly, what does your job entail?
   Secara ringkas, jelaskan bidang tugasana anda?

2. What is your role in financial disclosure decisions?
   Apakah peranan anda dalam pendedahan maklumat kewangan?

III. Disclosure Output (Hasil Pendedahan)
1. How does your council disclose financial information?
   Bagaimana PBT anda memdedahkan maklumat kewangan?

2. How does your council determine the form and content of your financial statement? Why?
   Bagaimanakah PBT anda menentukan bentuk dan kandungan penyata kewangan? Mengapa?

3. How frequent does your council disclose financial information? Why?
   Berapa kerapkan PBT anda mendedahkan maklumat kewangan? Mengapa?

4. What are the purposes of disclosure?
   Apakah tujuan pendedahan?

5. How does your local authority report financial information? Why?
   Bagaimana PBT anda melaporkan maklumat kewangan? Mengapa?

IV. Influences on financial information disclosure – Internal Antecedents
(Pengaruh dalam pendedahan maklumat kewangan – Anteseden Dalaman)

1. Does your local authority have a policy on financial information disclosure?
   Adakah PBT anda mempunyai polisi pendedahan maklumat kewangan?

2. How is the financial disclosure policy for your local authority decided?
   Bagaimanakah polisi pendedahan kewangan PBT anda ditentukan?

3. Do managers have discretion to make financial information disclosures in the annual report/financial statement or any other mediums of disclosure?
   Adakah pengurus diberi budi bicara untuk membuat pendedahan maklumat kewangan dalam laporan tahunan/penyata kewangan atau medium pendedahan lain?

4. Which managers have this authority and why are they given this authority?
Pengurus manakah yang diberi autoriti ini dan mengapa mereka diberi autoriti ini?

5. How does your local authority monitor and control what managers disclose in the annual report/financial statement or any other mediums of disclosure?
Bagaimankah PBT anda memantau dan mengawal apa yang didedahkan oleh pengurus bertanggungjawab dalam laporan tahunan/penyata kewangan atau medium pendedahan lain?

6. What other issues are considered when making disclosure decisions?
Apakah isu-isu lain yang diambil kira dalam membuat keputusan untuk pendedahan?

7. Why do they consider other issues mentioned in 6 above?
Mengapa isu-isu yang disebut dalam soalan 6 di atas diambil kira?

8. How are the disclosure decisions of managers in MLA influenced by issues mentioned in 6 above?
Bagaimanakah keputusan pendedahan oleh pengurus dipengaruhi oleh isu-isu yang dinyatakan dalam soalan 6 di atas?

VI. Influences on financial information disclosure –External Antecedents (Pengaruh dalam pendedahan maklumat kewangan – Anteseden Luaran)

1. How are the disclosure decisions of managers influenced by local authority norms (e.g. normal practice in the local authority)?
Bagaimanakah keputusan pendedahan pengurus dipengaruhi oleh norma PBT e.g. amalan norma PBT?

2. How are the disclosure decisions of managers influenced by external influences (e.g. legislations, standards and regulations)?
Bagaimanakah keputusan pendedahan pengurus dipengaruhi oleh pengaruh luaran e.g. undang-undang, standard dan peraturan?
3. How are the disclosure decisions of managers influenced by the existence of interorganizational networks (e.g. State authority, Ministry of Housing and Local Government)?

Bagaimanakah keputusan pendedahan pengurus dipengaruhi oleh kewujudan rangkaian antara organisasi e.g. Pihak Berkuasa Negeri, Kementerian Kewangan dan Kerajaan Tempatan?

VII. Influences of External Mediators (Pengaruh Pengantara Luaran)
1. What is the role of external auditor (e.g. Auditor General) in the financial disclosure of your local authority?

Apakah peranan juruaudit luaran e.g. Jabatan Audit Negara dalam pendedahan kewangan PBT anda?

2. How are the disclosure decisions of managers influenced by external auditors?

Bagaimanakah keputusan pendedahan pegurus dipengaruhi oleh juruaudit luaran?

3. How are the disclosure decisions of managers influenced by other professional consultants?

Bagaimanakah keputusan pendedahan pegurus dipengaruhi oleh perunding profesional yang lain?

4. How do other environmental influences affect disclosure decisions?

Bagaimanakah pengaruh persekitaran yang lain mempengaruhi keputusan pendedahan?

VIII. Usefulness/Adequacy of Disclosure (Kegunaan/Kecukupan Pendedahan)
1. What benefit(s) arise from the disclosure of financial information?

Apakah faedah yang diperolehi dari pendedahan maklumat kewangan?

2. Who are the beneficiaries of financial information disclosure?

Siapakah penerima pendedahan maklumat kewangan?
3. Do you think the needs of these beneficiaries are adequately met by financial disclosure?

Adakah anda merasakan bahawa keperluan penerima ini dipenuhi secukupnya dengan pendedahan maklumat kewangan?

4. Do you consider that the financial information needs of the public can be satisfied by means other than through financial statement? If so, in which way(s)?

Adakah anda merasakan keperluan orang awam terhadap maklumat kewangan boleh dipenuhi dengan pengantara lain selain dari penyata kewangan? Jika ia, apakah pengantara lain itu?
Appendix 5.3: University Ethics Approval

Memorandum

To
Neilson Anak Teruki, School of Accounting

From
Professor Zahirul Hoque, Chair, Faculty Human Ethics Committee

CC
Kamran Ahmed, School of Accounting

Subject
F-Final Approval. Ethics Application 05/10R
Incentives for Financial Disclosure: A case study of Malaysian Local Government

Date
16/04/2010

Dear Neilson,

The Faculty Human Ethics Committee (FHEC) has assessed your application as complying with the National Health and Medical Research Council’s National Statement on Ethical Conduct in Research Involving Humans and with University guidelines on Ethics Approval for Research with Human Subjects.

The FHEC Committee has granted approval for the period 01/04/2010 to 01/03/2012.

Please note that the FHEC is a sub-committee of the University’s Human Ethics Committee (UHEC). The decision to approve your project will need to be ratified by the UHEC at its next meeting. Consequently, approval for your project may be withdrawn or conditions of approval altered. However, your project may commence prior to ratification. You will be notified if the approval status is altered.

The following special conditions apply to your project: Approved Subject to the permission from the relevant research sites.

The following standard conditions apply to your project:

Complaints. If any complaints are received or ethical issues arise during the course of the project, researchers should advise the Secretary of the FHEC by mail or email:
FLM_ERGS@latrobe.edu.au

Limit of Approval. Approval is limited strictly to the research proposal as submitted in your application, while taking into account the conditions and approval dates advised by the FHEC.

Variation to Project. As a consequence of the previous condition, any subsequent variations or modifications you may wish to make to your project must be notified formally to the FHEC. Please submit to the FHEC secretary an Application for Approval of Modification to Research Project form (download from the UHEC website http://www.latrobe.edu.au/research-services/ethics/HEC-application.htm). If the FHEC considers that the proposed changes are significant, you may be required to submit a new Application Form.
**Progress Reports.** You are required to submit a *Progress Report* annually (if your project continues for more than 12 months) and/or at the conclusion of your project. The completed form (download from UHEC website [http://www.latrobe.edu.au/research-services/assets/downloads/HEC_Progress_and_Final_Report_Form.DOC](http://www.latrobe.edu.au/research-services/assets/downloads/HEC_Progress_and_Final_Report_Form.DOC)) is to be returned to the Secretary of the FHEC. Failure to submit a Progress Report will mean that approval for this project will lapse. An audit may be conducted by the FHEC at any time.

Your progress report is due by 01/02/2011 and a Final report is due by 01/04/2012.

If you have any queries, or require any further clarification, please contact me at the Faculty of Law and Management on 9479 1603, or by e-mail: [FLM_ERGS@latrobe.edu.au](mailto:FLM_ERGS@latrobe.edu.au)

Yours sincerely,

Professor Zahirul Hoque

Chair, Faculty Human Ethics Committee
PARTICIPANT INFORMATION SHEET

Research Title:

INCENTIVES FOR FINANCIAL DISCLOSURE: A CASE STUDY OF MALAYSIAN LOCAL GOVERNMENT

Ethics Approval No: 05/10R

Researcher: Neilson Anak Teruki, PhD (Accounting) candidate, School of Accounting, Faculty of Law and Management, La Trobe University, Victoria, Australia 3086. E-mail: nteruki@students.latrobe.edu.au

Supervisor: Professor Kamran Ahmed, Professor of Accounting, School of Accounting, Faculty of Law and Management, La Trobe University, Victoria, Australia 3086. Telephone: +613 9479 1125. E-mail: k.ahmed@latrobe.edu.au

Dear Sir,

Thank you for showing interest in participating in my PhD research entitled “Antecedents and Issues Influencing Disclosure: A Case Study of Malaysian Local Government”.

The purpose of this study is to investigate and to understand the financial disclosure practices and disclosure management in Malaysian Local Authorities (MLAs). This study is potentially useful to MLAs and the country in a number of ways. First, it is hoped that this study will provide the MLAs a better understanding of the issues surrounding financial disclosure. This understanding would be useful in directing local managers’ efforts towards perceived deficiencies in reporting. Secondly, the study would help regulators and policy making bodies to specify the form and content of accounting and reporting by local government councils. Lastly, the study would help other local authorities whose annual reporting might be inadequate.

The research will be conducted through a series of interviews with key people in your organization to discuss issues relating to financial disclosure practices and disclosure management in your organization. I also wish to view organisational documents which are related to financial disclosure, such as financial disclosure strategy/policy, the annual reports, and financial statements, and attend some of your meetings where issues of disclosure would be decided.

Your participation is voluntary and there will be no disadvantage or penalty for not participating or withdrawing from participation in this research.

You are invited to participate in this research by answering 10-15 interview questions. It will take approximately up to one hour to complete. Your feedback is important for my study in order to understand the practices and management of financial disclosure in your organization.
All data resulting from this study will be kept private. Information from interview transcripts will be confidential. Research files will be kept in lockable storage and only the researcher will have access to the files and be able to identify the interviewees. Data from this research will be used in my doctoral thesis and in later publications and conferences. You will not be identified by name, therefore your anonymity and confidentiality is assured.

If you have any questions, please contact me at nteruki@students.latrobe.edu.au, or my supervisor Professor Kamran Ahmed at k.ahmed@latrobe.edu.au.

If you have any complaints or queries that the investigator has not been able to answer to your satisfaction, you may contact: The Secretary, Faculty Human Ethics Committee, Faculty of Law and Management, La Trobe University, Victoria, 3086, Australia (ph: + 613 9479 3433) or email: FLM ERGS@latrobe.edu.au.

Yours sincerely,

Signature: Date:
Neilson Anak Teruki

PhD Supervisor:
Signature: Date:
Prof. Kamran Ahmed
Appendix 5.5: Translation of Participation Information Sheet

(PENYATA MAKLUMAT PENYERTAAN KAJIAN)

Tajuk Kajian:

FAKTOR – FAKTOR YANG MENDORONG PENDEDAHAN MAKLUMAT KEWANGAN: KAJIAN KES DI PIHAK BERKUASA TEMPATAN DI MALAYSIA

No Kelulusan Etika: 05/10R

Penyelidik: Neilson Anak Teruki, Calon PhD (Perakaunan), Sekolah Perakaunan, Fakulti Undang-Undang dan Pengurusan, La Trobe University, Victoria, Australia 3086. E-mail: nteruki@students.latrobe.edu.au

Penyelia: Professor Kamran Ahmed, Professor Perakaunan, Sekolah Perakaunan, Fakulti Undang-Undang dan Pengurusan, La Trobe University, Victoria, Australia 3086. Telefon: +613 9479 1125. E-mail: k.ahmed@latrobe.edu.au

Tuan/Puan,

Terima kasih kerana menyertai kajian PhD saya bertajuk “Faktor-Faktor Yang Mempengaruhi Pendedahan Maklumat Kewangan: Kajian di Pihak Berkuasa Tempatan di Malaysia”.


Penglibatan anda dalam kajian ini adalah secara sukarela dan tiada apa-apa tindakan akan diambil sekiranya anda tidak berminat atau menarik diri dari menyertai kajian ini.


Sekiranya anda mempunyai sebarang pertanyaan, anda boleh menghubungi saya di alamat e-mail nteruki@students.latrobe.edu.au, atau penyelia saya, Professor Kamran Ahmed di k.ahmed@latrobe.edu.au.

Sekiranya anda mempunyai aduan atau tidak berpuashati dengan penjelasan terhadap pentanyaan anda oleh penyelidik, anda boleh menghubungi: Setiausaha, Jawatankuasa Fakulti Etika Kemanusiaan, Fakulti Undang-Undang dan Pengurusan, La Trobe University, Victoria, 3086, Australia (ph: + 613 9479 3433) atau email: FLM ERGS@latrobe.edu.au.

Yang Benar,

Tandatangan:__________________________ Tarikh:__________________________

Neilson Anak Teruki

Penyelia PhD:

Signature:__________________________ Tarikh:__________________________

Prof. Kamran Ahmed
Appendix 5.6: Consent Form

CONSENT FORM

ETHICS APPROVAL NO: 05/10R

Research Title:
ANTECEDENTS AND ISSUES INFLUENCING DISCLOSURE: A CASE STUDY OF MALAYSIAN LOCAL GOVERNMENT

In order to participate in this study, this Consent Form must be signed by the participant.

I ________________________________________ have read and understood the Participation Information Sheet and consent form, and any questions I have asked have been answered to my satisfaction. I agree to participate in this project, realising that I may physically withdraw from the study at any time and may request that no data arising from my participation are used, up to four weeks following the completion of my participation in the research. I agree that research data provided by me or with my permission during the project may be included in a thesis, presented at conferences and published in journals on the condition that neither my name nor any other identifying information is used.

If you have any questions regarding this study you may contact Neilson Anak Teruki, of the School of Accounting, Faculty of Law and Management, La Trobe University, Bundoora 3086 Melbourne Australia. If you have any complaints or queries that the researcher has not been able to answer to your satisfaction, you may contact Professor Kamran Ahmed (Supervisor) at k.ahmed@latrobe.edu.au or Secretary, Faculty Human Ethics Committee, Faculty of Law and Management, La Trobe University, Victoria, 3086, Australia (ph: + 613 9479 3433) or email: FLM_ERGS@latrobe.edu.au.

Name of Participant (block letters): ____________________________________________

Signature: __________________________________________________________________
Date: ___________________________________________________________________

Name of Investigator (block letters): NEILSON ANAK TERUKI

Signature: __________________________________________________________________
Date: ___________________________________________________________________

Name of Student’s Supervisor (block letters): PROFESSOR KAMRAN AHMED

Signature: __________________________________________________________________
Date: ___________________________________________________________________
Contact details:

Neilson Anak Teruki, PhD (Accounting) candidate, School of Accounting, Faculty of Law and Management, La Trobe University, Victoria, Australia 3086.
Telephone: +614 33562060. E-mail: nteruki@students.latrobe.edu.au

Professor Kamran Ahmed, Professor of Accounting, School of Accounting, Faculty of Law and Management, La Trobe University, Victoria, Australia 3086.
Telephone: +613 9479 1125. E-mail: k.ahmed@latrobe.edu.au
Appendix 5.7: Translation of Consent Form

BORANG KEBENARAN

NO KELULUSAN ETIKA: 05/10R

Tajuk Kajian:

FAKTOR – FAKTOR YANG MENDORONG PENDEDAHAN MAKLUMAT KEWANGAN: KAJIAN KES DI PIHAK BERKUASA TEMPATAN DI MALAYSIA

Untuk menyertai kajian ini, Borang Kebenaran ini perluah ditandatangani oleh peserta.

Saya ________________________________________ telah membaca dan memahami Penyata Maklumat Penyertaan Kajian dan Borang Kebenaran, dan saya berpuashati dengan setiap penjelasan mengenai persoalan berkaitan. Saya bersetuju untuk menyertai projek ini, memahami bahawa saya boleh menarik diri dari kajian ini pada bila-bila masa dan saya berhak meminta untuk tidak menggunakan data daripada penyertaan saya untuk digunakan, sehingga empat minggu selepas penyertaan saya dalam kajian ini. Saya bersetuju bahawa data kajian yang saya berikan atau dengan keizinan saya dalam projek ini mungkin digunakan di dalam tesis, dipersembahkan dalam persidangan dan diterbitkan dalam jurnal berlandasan syarat tiada nama saya atau maklumat pengenal diri digunakan.

Sekiranya anda mempunyai sebarang persoalan mengenai kajian ini, anda boleh menghubungi Neilson Anak Teruki, dari Sekolah Perakaunan, Fakulti Undang-Undang dan Pengurusan, La Trobe University, Bundoora 3086 Melbourne Australia. Sekiranya anda mempunyai aduan atau tidak berpuashati dengan penjelasan terhadap pentanyaan anda oleh penyelidik, anda boleh menghubungi Professor Kamran Ahmed (Penyelia) di alamat e-mail k.ahmed@latrobe.edu.au atau Setiausaha, Jawatankuasa Fakulti Etika Kemanusiaan, Fakulti Undang-Undang dan Pengurusan, La Trobe University, Victoria, 3086, Australia (ph: + 613 9479 3433) atau e-mail: FLM_ERGS@latrobe.edu.au.

Nama Peserta (Huruf Besar): ______________________________________________

Tandatangan: 

Tarikh: 

Nama Penyelidik (Huruf Besar): NEILSON ANAK TERUKI

Tandatangan: 

Tarikh: 

Nama Penyelia kepada Penyelidik (Huruf Besar): PROFESSOR KAMRAN AHMED

Tandatangan: 

Tarikh: 

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Butir-Butir Perhubungan:

Neilson Anak Teruki, Calon PhD (Perakaunan), Sekolah Perakaunan, Fakulti Undang – Undang dan Pengurusan, La Trobe University, Victoria, Australia 3086. Telefon: +614 33562060. E-mail: nteruki@students.latrobe.edu.au

Professor Kamran Ahmed, Professor Perakaunan, Sekolah Perakaunan, Fakulti Undang – Undang dan Pengurusan, La Trobe University, Victoria, Australia 3086. Telefon: +613 9479 1125. E-mail: k.ahmed@latrobe.edu.au
Appendix 6.1: Local Authority Name in Abbreviation

<table>
<thead>
<tr>
<th>Local Authority’s Name</th>
<th>Abbreviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alpha</td>
<td>KKA</td>
</tr>
<tr>
<td>Beta</td>
<td>JJB</td>
</tr>
<tr>
<td>Gamma</td>
<td>SSG</td>
</tr>
<tr>
<td>Delta</td>
<td>LLD</td>
</tr>
<tr>
<td>Omega</td>
<td>AAO</td>
</tr>
</tbody>
</table>
References


