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Ibrahim Mohd-Sabrun & Rusnah Muhamad

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Do environmentally sensitive companies engage in lesser earnings management behaviour? evidence from Malaysia

Ibrahim Mohd-Sabrun [a] and Rusnah Muhamad [b]

[a]Department of Accounting, Faculty of Economics and Business, Universiti Malaysia Sarawak, Kota Samarahan, Malaysia; [b]Department of Accounting, Faculty of Business and Economics, Universiti Malaya, Kuala Lumpur, Malaysia

ABSTRACT

Past studies have examined the influence of environmental information on earnings management practices. However, these studies have reported mixed findings and failed to establish a conclusive conclusion. Therefore, rather than re-examining the relationship between environmental disclosure and earnings management, this research offers a new perspective on earnings management based on a company's sector, specifically, environmentally sensitive (ES) and environmentally non-sensitive (EN) sectors. This study analysed ten years of data (2008–2017) on Malaysian public listed companies. It was found that ES sectors are more likely to be involved in earnings management than EN sectors. This study's findings could initiate policy revisions leading to sustainable, ethical and responsible financial reporting practices in the future.

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KEYWORDS
Earnings management; Earnings manipulation; Environmentally sensitive sectors

1. Introduction

Earnings management generally involves altering a company's financial statements by structuring transactions (Dechow, Sloan, and Sweeney 1995; Beneish 1999). On the one hand, these practices seem to be aligned with accounting regulations and standards, while on the other, scholars have argued that earnings management practices constitute several manipulation methods (Roychowdhury 2006; Coffee 2005; Petrovits 2006). Such practices could negatively affect a nation's economic landscape and financial outcome (Graham, Harvey, and Rajgopal 2005).

Companies' self-indulgence exacerbated by pernicious accounting manipulation has led to financial scandals like Andersen, Enron, and Worldcom, which are linked to the collapse of financial markets and economic crises. Due to their severity, regulatory reforms have been made to avoid these scandals (Coffee 2005). This situation raises the concern over whether a financial crisis is the only way to reform financial reporting and accounting standards?

Theoretically, companies with better financial performance are more inclined to disclose comprehensive environmental information, possibly intended for financial success

CONTACT Ibrahim Mohd-Sabrun imsabrun@unimas.my Department of Accounting, Faculty of Economics and Business, Universiti Malaysia Sarawak, Kota Samarahan, Sarawak, Malaysia
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