ISSN: 2277-3878, Volume-7, Issue-6S3, April 2019

Corporate Frauds in Emerging Markets: Cases Involving Malaysia Companies

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I. Introduction:

Despite the established need of business ethics for companies, the wave of corporate scandal is still in rise in Malaysia. Malaysia is unique as an Asian country due to its institutional environment. Survey conducted by KPMG from 2013-2014 shows that fraud is still a major issue in Malaysia. The survey shows that 89% of Chief Executive of Malaysian PLC acknowledge that fraud has risen over the past 3 years. Fraud investigation by Ernst and Young (2013) also confirms that Malaysia is inclined to corporate frauds [1][9][15].

The reason for choosing Malaysia as the background of this study is because Malaysia is able to project growths in its economics. According to Department of Statistics Malaysia (2013), Malaysia's GDP has increase to 6 percent per year [6][11].

In Malaysia, Transmille Group Bhd's audit has caused public to be doubtful in the ability of accountants in checking and verifying the accounts. This is due to the fact that there is accounting irregularities and fraud in the company's accounts. The company has overstated its accounts in two consecutive years in 2005 and 2006. The company was making loss and this loss was not detected by its auditors Deloitte & Touche. Apart from that, the audit of Ocean Capital Bhd which also was audited by Deloitte & Touche. Deloitte & Touch didn't inform Ocean Capital's shareholders that the company is making loss since the year 2000 .

II. Fraud cases in Malaysia from 1998-2010:

No	Companies	Year of Revelation	Annual Audited Accounts	Quarterly Reports	Listing Proposal/ IPO Prospects	Corporate Restructuring Proposal
1	Zaitun	1998/ 2000	1997 / 1999			
2	Ganad	2001			1998	
3	Tat Sang	2002	2000			
4	Aktif Lifestyle	2005	2004			
5	Goh Ban Huat	2005		4^{th} Q 2004		
6	Ocean Capital	2005				2003
7	Oilcorp	2005	2003			
8	Omega	2005				2003
9	GP Ocean Food	2006			2006	
10	Granasia	2006			2006	
11	Hospitech	2006			2006	
12	Polymate	2006	2005			
13	Megan Media	2007		3^{rd}Q 2007		
14	Nasion Com	2007	2005		2004	
15	Southern Bank	2007	2005			
16	Transmile	2007	2004 - 2006			
17	United U-Li	2007	2004			
18	Welli Multi	2007	2005	1-3^{rd}Q 2006		
19	Wimems	2007	2005		2005	

20	LFE	2008		1-4thQ 2007		
21	Satang	2008		1-4thQ 2007		
22	MEMS Technology	2009	2007 / 2008	1st/2nd Q 2009		
23	Inix Technologies	2010		1-4thQ 2006	2005	

Source: Chee Kwong Lau Ki Wei Ooi (2016)

The above table shows that financial reports are manipulated into four aspects: yearly accounts, quarterly reports, financial accounts listed in IPO and corporate proposals. Most of these fraud are detected several years after occurrence. Fraud are also detected in interim reports example MEMS Technology company [10].

III. Literature Review:

To support the literature aspect of this study, I am using Kohlberg's Theory of Moral Development which is linked to ethical behavior of an individual [7]. Kolhberg's theory of moral development can be grouped into three phases namely pre-conventional, conventional and post-conventional. During this pre-conventional phase individuals will obey rules that are laid down[8].

Apart from that, in this phase self-interest is also involved when choices are given to make alternatives where individual is prompt in rewarding themselves by choosing the terms that could bring personal benefit. Whereas in the conventional phase individual draws concerns on what does the society perceived about them. Therefore, individuals will tend to act with loyalty and ensure fairness in making judgments. In the post-conventional phase, individual is believed to adopt the inner conscience where tolerance aspect is given a room here .

Level	Morality defined	Stage	Moral Motivation
Pre-Conventional	Self-centred	1	Obedience, avoidance of punishment, self-interest, gain rewards
	ethics	2	
Conventional	Social group	3	Good interpersonal relationship, should live up to the expectations
		4	Adherence to legal and moral Codes/maintaining social order
Post-Conventional	Universal Ethics Principal	5	Social contract and individual's right
		6	Self-chosen ethical principles

Source: (Kohlberg, 1984)

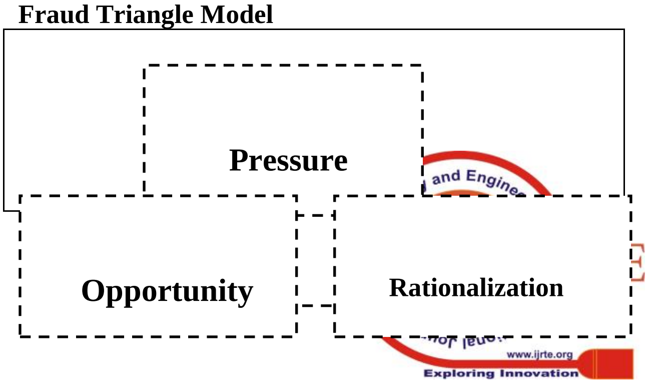
The Pre-Conventional level is also defined as the self-centered ethics. In this first stage, an individual will tend to avoid punishment. Individual will tend to be responsible for his or her action as the outcome of the action will determine whether or not the individual receive or avoid punishment. In the second stage, self-interest serves as a dominating factor. This is due to this stage tends to satisfy the third person where one is expected to have personal gains. The pre-conventional level is belief to test the patience of an individual [3][4].

Accountants' independence is truly based on the client even though some auditors are highly sensible to ethics .

The second level of moral reasoning is the conventional ethics. In this stage, accountants tend to act in accordance with the guided rules and regulations. This is because the focus of this second level is strongly based on the society's perception and view about the features of the conventional morality. The third stage in Kohlberg's Six Stages is post-conventional where individual tend to act in accordance with the roles identified by their societies. In this stage, accountants tend to be as good as possible in order to live up to the expectation of their society by preparing true and fair accounts.

The fourth stage in Kohlberg's Six Stages is compliance to authority. In this stage, accountants are expected to obey the law, dictums and social conventions. The morality level in this stage is seen as advanced compared to the previous stage as individual learn to surpass for their own needs . The fifth stage tends to emphasized on the social contracts which is been implanted in the third stage itself. The highest level in Kohlberg's Theory is the post-conventional level. In this level, accountants are expected to be able to distinguish what is right and wrong as they aware of their rights and understand the ethical principles that they want to adopt. The focus area of stage six is the universal ethical principles where accountants are governed to follow or obey the law. Any disobedience to the law will not be tolerated. Kohlberg emphasized on this stage as he felt that this is the most important stage that an accountant should uphold but in reality it is difficult to find someone who really follow this.

Fraud Triangle Model



Published By: Blue Eyes Intelligence Engineering & Sciences Publication

ISSN: 2277-3878, Volume-7, Issue-6S3, April 2019

Source: Cressy (1953)

In 1950, Cressy has investigated what drives a person to commit fraud. He has introduced three main reasons which cause an individual to engage in fraud which is pressure, opportunity and rationalization. Pressure can be defined as factors which cause a person to act in unethical manner. These pressure can be in the form of financial or non-financial. 95% of the fraud cases is due to financial pressure [2][5].

Pressure also can be related as employees willingness to involve in fraud due to financial pressure (Rae and Subramanian, 2008). Similarly, Vona (2008) and Rasha and Andrew (2012) agrees that individual commit frauds due to personal and corporate pressures[13].

The second element that caused a fraud to occur is opportunity. Organizational fraud exist because of ineffective internal control. In accounting terms this is known as weak internal control. Opportunity propose that individuals will make use of the situations that is advantages to them in order to commit fraud .Opportunity to commit fraud in organization is also due to negligence (Sauser, 2007). Rae and Subramanian (2008) agrees that weak internal control encourage employees to engage in fraudulent activities[12].

The third element that caused a fraud to occur is rationalization. Rationalization is the justification to engage in an unethical behaviour. Individuals who are engaged in fraud are able to justify their action are right. For example: " I am just taking the money that was supposed to be paid to me as an increment". Employees tend to justify their act to commit fraud because employer didn't provide increment (Hooper and Pornelli, 2010).

IV. Research Design:

The data were collected from enforcement action releases (EAR) company announcements to the Bursa Malaysia.

V. Findings and Discussions:

The fraudulent financial reporting cases has last for twelve years continuously from the year of 1998-2010 in Malaysia. The financial reports are manipulated in four aspects namely yearly accounts, quarterly reports, financial reports and corporate proposals. Seven companies has manipulated its financial reports contained in IPO related documents. In order to meet the minimum threshold for listing proposals, Granasia Company has created bogus sales for its financial statements. Moreover, Inix companies' initial offerings were oversubscribed by 17.9

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