Journal of
Empirical Research In Accounting

**Alzahra University, Faculty of Social Sciences and Economics**
**Empirical Research in Accounting, Spring 2024, V. 14, No. 51, pp.47-50**

# Investigating the Role of Corporate Governance Principles on Earnings-Increasing or Decreasing Choices by Management[1]

**Hadise Nasiri Alamoti[2], Alireza Mehrazeen[3], Abolghasem Masihabadi[4], Mohammad Heydari[5]**

Received: 2023/10/30
Accepted: 2024/01/27

Research Paper

## INTRODUCTION

Agency theory is considered as the concept originator of the corporate governance principles. Corporate management principles consist of extensive organizational mechanisms that are effective in reducing agency problems through managerial actions and opportunistic behavior of managers, improving the quality of information (Ramli and Rashid, 2010). The conflict of interest arising from agency theory between managers and users affects the choice of methods and determination of company methods by management (Huang et al., 2016). Discretion for managers in accounting reports related to accounting literature is called accounting choices that can increase or decrease the company's earnings. (Fields et al., 2001) According to the explanations of why this research was conducted and its innovation, the importance of the research can be examined from two perspectives:

First of all, by reviewing the literature and internal studies, it can be seen that three studies have been conducted (Eyvazi Heshmat, 2007; Hassas Yeganeh and Karimi, 2011; Moradi, 2020) with very limited aspects, focusing on one accounting method and they have dealt with this issue qualitatively.

---

1. DOI: 10.22051/JERA.2024.45416.3178
2. Department of Accounting, Neyshabur Branch, Islamic Azad University, Neyshabur, Iran. (Nasirialamoti@gmail.com).
3. Department of Accounting, Neyshabur Branch, Islamic Azad University, Neyshabur, Iran. (Corresponding Author). (a.r.mehrazeen@iau-neyshabur.ac.ir).
4. Department of Accounting, Neyshabur Branch, Islamic Azad University, Neyshabur, Iran. (massihabadi@gmail.com).
5. Department of Economics, Neyshabur Branch, Islamic Azad University, Neyshabur, Iran. (mheidar20006@yahoo.com).

Second, conducting this research can be of great help to standard developers and investors. The development of standards that provide the basis for the selection of methods by managers can lead to different decisions by decision-makers. Therefore, the purpose of this research was to investigate the effect of corporate governance principles as one of the effective factors on the choice of accounting methods by managers on earnings-increasing or decreasing.

## METHODOLOGY

This research was based on the correlation method with the regression approach in terms of the use purpose. The statistical population included manufacturing companies listed in the Tehran Stock Exchange from the beginning of 2014 to the end of 2021. The selected sample had the following conditions: First, the companies were not among banks and financial institutions (investment, holding, and leasing companies). Second, the required financial information should be available during the research period. Third, the company's stock transactions should be done continuously. Fourth, there is no suspension of transactions for more than three months in the mentioned period, and their fifth fiscal year ended on December 29. According to these conditions, 180 sample companies (1440 company-years) were selected and prepared as panel data for hypothesis testing in the research. The variables included three categories dependent variables (accounting choices), independent variables (corporate governance principles), and control variables (investment opportunities set, good and bad news, financial leverage, and industry). In this research, accounting choices were considered a dummy variable in which the method of earnings increase took one while the method of earnings decrease took zero. In this study, five methods were selected that could increase or decrease earnings, including: (Ⅰ) valuation of inventory, (Ⅱ) valuation of long-term investments in subsequent recognition, (Ⅲ) depreciation of fixed assets, (Ⅳ) valuation of property, plant and equipment, (Ⅴ) employee retirement benefits. In each company, a composite measurement score was calculated based on the type and number of methods used by the company. Companies must have used at least two methods to be counted in this scoring. Data analysis was done using Stata. To explain the variable effect of accounting choices on principles of corporate governance, the research of Astami and Tawar, (2006) and Meissonier (2004) was used:

$$AC_{it} = \beta_0 + \beta_1 CG_{it} + \sum_{i=1}^{4} control + e_{\mathrm{it}}$$

Where,

$AC_{it}$ : Accounting choices for the company (i) in the year (t)

$CG_{it}$ : Principles of corporate governance for the company (i) in the year (t),

$\sum_{i=1}^{4} control$ : Control variables, such as financial leverage, good and bad news (GBN), investment opportunity set (IOS), industry, and $e_{\mathrm{it}}$ as residuals.

## RESULTS AND DISCUSSION

The findings showed that the principles of corporate governance can have a positive and significant effect on the selection of earnings-increasing or decreasing methods. In other words, managers in companies with strong corporate governance principles tended to use earnings-increasing methods while, managers in companies with weak corporate governance principles tended to use earnings-reducing methods. This means that strong corporate governance principles increase the motivation of managers to access confidential information of the company for personal benefits, because they have been able to attract the attention of institutions (tax, political, and regulatory). After all, the company has been able to achieve its desired results to some extent. to achieve Therefore, managers in these companies tend to make earnings-increasing choices, while weak corporate governance principles, due to lack of transparency and information disclosure, provide a ground for the company to leave the competition market, which leads to a decrease in sensitivity and attention from political institutions. Some motivations for choosing methods are created as a result of the political process. The use of earnings figures by politicians and legislators has motivated company managers to use accounting methods that reduce earnings. Therefore, if the managers of the companies see that they are not at the center of political attention, they will adapt the accounting method to show the earnings of the company less. This result is in line with the research findings of Missonier, (2004); Astami and Tower, (2006); Waweru et al., (2011); and Jahangir and Kamran (2017) do not match.

## CONCLUSION

According to the results of the research, it is suggested that the auditing organization formulate standards or provide solutions to limit the possibility of method choice of managers in financial statements and in this way reduce the scope of opportunism of managers in line with personal interests to the minimum possible level. It is also recommended that the standard setters pay special attention to the accounting methods chosen by the managers so that they can provide a better view to the decision-makers in this regard.

The limitation of this research was related to the mechanisms of corporate governance principles. In several companies, the intended mechanisms in the research were not properly disclosed and this led to a decrease in the number of samples. In the end, future researchers are suggested to examine the effect of managers' behavioral characteristics on accounting choices in the form of behavioral research and examine the effect of other influencing factors, such as company size, type of industry, etc. on accounting choices.

**Keywords:** Choice of Accounting Methods, Corporate Governance Principles, Earnings Increasing or Decreasing Methods.

**JEL Classification:** A19, M41.