African development finance journal http://journals.uonbi.ac.ke/index.php/adfj
July Vol4 No.2, 2020 PP 79- 95 ISSN 2522-3186

CORPORATE GOVERNANCE AND EARNINGS MANAGEMENT OF COMPANIES LISTED AT NAIROBI SECURITIES EXCHANGE

Veronica Nyatichi[1], Cyrus Iraya (PhD)[2], Mirie Mwangi (PhD)[3] and James Njihia (PhD)[4]

Abstract

Purpose: *The purpose of the study was to establish the relationship between corporate governance and earnings management of companies listed at the Nairobi Securities Exchange.*
Methodology: *The study employed a correlational descriptive research design. Panel data methodology that incorporates both time series and cross-sectional analysis techniques was utilised. The study sample included 56 listed companies for period 2008 to 2017 and secondary data was utilised for data collection. The data collected was analyzed through descriptive technique and multiple regression models were utilized to test the hypothesis.*
Findings*: The study findings revealed that board size had a statistically significant negative effect on earnings management. Overall, the results indicated that corporate governance significantly influeces earnings management of companies listed at the Nairobi Securities Exchange.*
Implications*: The results imply that for firms to effectively monitor the earnings management practices the size of board of directors should be large.*
Value*: The study adds value to the regulators of listed companies who develop corporate governance principles by providing evidence on how board of directors is an important component of governance. It specifically guides the regulators to understand that size of board plays a key role in monitoring firm activities.*
This paper contributes to the current knowledge in the areas of corporate governance and earnings management practices

Key words: *Corporate governance, earnings management, discretionary accruals, board of directors.*

[1] Department of Finance and Accounting , School of Business, University of Nairobi.
[2] Professor, Department of Finance and Accounting , School of Business, University of Nairobi.
[3] Professor, Department of Finance and Accounting , School of Business, University of Nairobi.
[4] Professor, Department of Management Science, School of Business, University of Nairobi.

July Vol4 No.2, 2020 PP 79- 95 ISSN 2522-3186

1. Introduction

Despite the continuous emphasis being placed on corporate governance as a device for safeguarding shareholders wealth, cases of corporate scandals are still rife both internationally and locally. Internationally, they include Enron, WorldCom and Ahold in the USA (Norwani, Mohamed & Chek,2011) and bankruptcy of Pramuka Bank of Sri Lanka among others (Kalainathan & Vijayarani, 2014). Locally, placement of Imperial Bank on receivership in 2015 was largely attributed to misrepresentation of financial statements (CMA, 2015a). Dubai Bank was closed in 2015 and Chase bank placed under receivership and subsequenrtly closed in 2016 due to weak corporate governance and failure to maintain adequate capital and liquidity ratios (CBK, 2015). These corporate governance challenges in Kenyan companies was the motivation for this study. It sought to determine the relationship between corporate governance and earnings management.

Weak governance structures provides managers with opportunity to engage in behaviors that would lead to lower quality of reported earnings, that indicates decay in business ethics (González & García-Meca, 2014). The uncovering of accounting fraud in stock markets in the years 2001 in Enron and 2002 in WorldCom resulted to development of guidelines on corporate governance in various countries as a response to corporate scandals (Larcker, Richardson & Tuna, 2007). The responses entailed measures to protect transparency of information, reduce disagreement between shareholders and management and warrant auditors independence. In Kenya, the first document of rule based guidelines on corporate governance practices were issued by Capital Markets Authority in 2002 under gazette notice No. 3362. This was later amended in 2015 under gazette notice number 1420 to principle based guidelines on corporate governance practices (CMA, 2015_b). The current approach recognises satisfactory explanation and full disclosure of any non-compliance with the code guidelines by the board. In addition, corporate governance guidelines promotes board members independence and eliminates idea of duality on board chairman and chief executive officer positions (CMA, 2015_b).

Although studies such as Latif and Abdullah (2015); Buniamin, Johari, Rahman, and Rauf (2012); Nugroho and Eko (2011); Bekiris and Doukakis (2011) among others have determined how earnings management is influenced by corporate governance, their studies relate to countries such as USA, Europe, Pakistan, Indonesia and Malaysia whose economy are considered developed. Minimal studies have been conducted on developing economy nations which have different macro level factors in comparison to developed countries. These studies on relationship between corporate governance and earnings management have also had conflicting results (Latif & Abdullah, 2015; Buniamin et al., 2012; Waweru, & Riro,2013; Iraya, Mwangi &Muchoki , 2015). For example, Waweru and Riro (2013) concluded that

when ownership concentration of a firm increases its earnings management practices increases. This is contrary to Iraya et al. (2015), findings that established an increase in ownership concentration, board independence and size decreases practice of earnings management. In addition, Nugroho and Eko (2011) results indicated independence of board members and size had no direct influence on earnings management practices. In order to address these gaps, this study attempted to establish relationship between corporate governance and earnings management of listed companies in Kenya by focusing on board of directors as component of corporate governance. This was done through answering the question: is there relationship between corporate governance and earnings management of companies listed at Nairobi Securities Exchange?

2. Literature Review

This section outlines the theories that backed the study and the empirical review of studies in relation to corporate governance and earnings management.

Dey (2008) documents that agency conflict arises from segregation of control and ownership, presence of information asymmetry among shareholders and managers, divergent management and shareholder objectives. These agency conflicts enable managers to have motivation and power to enhance their individual benefits at cost of corporate shareholders hence leading to earnings management. The ability to resolve such agency conflicts can only be effective through establishment of corporate governance structures in the organization. Dey (2008) further explains that the governance structure of a firm involves mechanism to minimize agency conflicts. This means that if the degree of conflict is high a stronger governance structure should be put in place in comparison to when degree of conflict is low. The agency theorist viewed management compensation contracts as a tool that can be used for reduction of interest conflicts between shareholders and managers (Sun, Liu & Lan, 2011).

Lasdi (2013) indicates that information asymmetry occurs when information about the business internal affairs and future company's prospects are well known by the managers as compared to stakeholders. Corporate governance has been regarded as a monitoring mechanism effective in resolving difficulties of information asymmetry among stakeholders and managers. The main way that corporate governance resolves information asymmetry is by establishment of board of directors who are independent and who are mandated to observe the work of executive directors.

Abed, Al-Attar & Suwaidan (2012) in his study analysed association between earnings management and corporate governance characteristics for listed firms at Jordan and concluded that relationship between percentage of board independence, duality and insider ownership on

earnings management was not significant while association between board size and earnings management was significantly negative.

Liu, Harris & Omar (2013) study established impact of board and sub-committees on restraining earnings management practices at Australian listed companies. The findings were audit committee independence, existence of nomination committee and frequency of meetings are linked with earnings management negatively. The influence of corporate governance on earnings management for firms listed in Athens, Milan and Madrid was done by Bekiris and Doukakis (2011). The results revealed that firms which had good corporate governance standards practised earnings management at minimal level as compared to those with lower levels of corporate governance standards.

Gulzar and Wang (2011) researched on correlation between corporate governance characteristics and earnings management for listed firms in China at Shenzhen and Shanghai. The documented findings indicate that corporate governance characteristics like segregation of CEOs and chairman role, female directors' proportion, number of meetings and concentrated ownership are inversely linked with earnings management.

Okougbo and Okike (2015) analysed the link between corporate governance and earnings management for listed companies in Nigeria Stock exchange. Using content analysis on 62 selected non-financial listed companies, their findings revealed that firms of small board size had lower practices of earnings management as compared to ones whose board size was large. Most firms engaged in downwards earnings management practices as compared to upward discretionary accruals practices this is due to the need to use current profits to cover for future losses.

Iraya et al. (2015) analysed relation between corporate governance and earnings management of listed companies at NSE. Their findings indicated that ownership concentration, size of board and board independence decreases earnings management. In contrast, earnings management is influenced upwards by number of meetings held and when there is duality of CEOs position.

Buniamin et al., (2012) analysed impact of board diversity on earnings management. Documented results revealed that correlation between women on board and discretionary accruals was positive, association between cash flows and discretionary accruals was negative while link between board independence, competence, remuneration and earnings management was not significant.

3. Methodology

Positivism philosophy was exploited to statistically establish association between corporate

governance and earnings management of listed firms at NSE using multiple regression models because it is dependent on observations that can be quantified. This study utilized a correlational descriptive research design and panel data methodology that incorporates both time series and cross-sectional analysis techniques were also utilized as this enabled the researcher to focus on the period of the study that had observable data.

The study population was all listed firms at NSE as at 31st December 2017. From years 2008 to 2017 a sample of 56 companies with 517 firm year end observations were identified and utilized for data analysis. Secondary data was appropriate as compared to primary data because data for all the variables of the study were available in the companies' published financial reports. For this study, data for computation of earnings management and corporate governance measures were collected from corresponding companies' financial reports which were available at CMA website and NSE handbook.

4. Results

This section discusses the data analysis results and hypothesis testing.

4.1 Earnings management model

Earnings management presence in the financial statements was determined by accruals that vary depending on accounting choices made by managers. Gavious, Segev and Yosef (2012) define accruals as short-term adjustments that solves problem of timing in the current cash flows at an expense of creating estimates and assumptions. Accruals include all amendments which allow companies to move from an approach of cash whether it entails making changes in working capital, allocations, and changes in accounting methods or provisions.

Discretionary accruals are considered best determinant of earnings management since they represent intervention that management has done during the process of preparing financial reports (Lakhal, Aguir, Lakhal & Malek, 2015). They are determined by deducting non-discretionary accruals from total accruals. When using discretionary accruals as estimate of earnings management aspects of non-discretionary accruals are omitted as they reflect business conditions that are subject to firm's condition which managers cannot control (Gavious et al., 2012). Modified Jones (1995) model has been regarded as the most reliable way of identifying managerial discretion over accounting choices by various researches (Lakhal et al., 2015; Iraya et al., 2015. For computation of discretionary accruals, the study utilized modified Jones model.

The first step of model was to use cashflow approach to determine the total accruals as shown in equation 1:

July Vol4 No.2, 2020 PP 79- 95 ISSN 2522-3186

$$TA_{jt} = NI_{jt} - OCF_{jt} \text{ ----------(1)}$$

Where:

TA_{jt} is total accruals for firm j in year t.

NI_{jt} is net income for firm j in year t.

OCF_{jt} is operating cash flow for firm j in year t.

The second step was to compute non-discretionary accruals. Before its computation, the model parameters were determined using equation 2.

$$\frac{TA_{jt}}{A_{jt-1}} = \beta_0\left(\frac{1}{A_{jt-1}}\right) + \beta_1\left(\frac{\Delta REV_{it} - \Delta REC_{it}}{A_{jt-1}}\right) + \beta_2\left(\frac{PPE_{jt}}{A_{jt-1}}\right) + \varepsilon_{jt} \text{ ----------(2)}$$

Where:

NDA_{jt} is non-discretionary accrual for firm j in year t

A_{jt-1} is total assets for firm j in year t-1

ΔREV_{jt} is change in net revenue for firm j in year t

PPE_{jt} – is gross property, plant and equipment for firm j in year t

ΔREC_{jt} is change in accounts receivable for firm j in year t

β_0, β_1, β_2 are coefficients.

The summary of the regression model 2 as shown in Table 1 was used to ascertain parameters of non-discretionary accruals for listed companies at Nairobi Securities Exchange.

Table 1: Overall Non-Discretionary Accruals Coefficients

Variable	Coefficient	Std. Error	t-Statistic	Prob.
β_0	0.297334	0.056502	5.262375	0.0000
β_1	0.028261	0.013114	2.155134	0.0316
β_2	-0.081237	0.012224	-6.645524	0.0000

R-squared	0.085447
Adjusted R-squared	0.081888
S.E. of regression	0.125814
Sum squared resid	8.136245
Log likelihood	339.6269
Durbin-Watson stat	1.839684

Dependent Variable: Total Accruals
Method: Panel Least Squares
Sample: 2008 2017
Periods included: 10

Cross-sections included: 56
Total panel (unbalanced) observations: 517
Source: Author (2020)

As per Table 1 all the independent variables of model 2 were significant as their p values were less than 0.05. There variables did not depict any autocorrelation problem. This is revealed by the results of Durbin Watson Statistics which is 1.83. The value lies within two critical values of $1.5 < d < 2.5$ which is an indication of no auto correlation. The values of the coefficient of β_0 was 0.297334, β_1 was 0.028261 and β_2 was (0.081237). These coefficients were replaced in equation 3 below to determine the non-discretionary accruals.

$$\frac{NDA_{jt}}{A_{jt-1}} = \beta_0\left(\frac{1}{A_{jt-1}}\right) + \beta_1\left(\frac{\Delta REV_{it} - \Delta REC_{it}}{A_{jt-1}}\right) + \beta_2\left(\frac{PPE_{jt}}{A_{jt-1}}\right) \text{ ---------- (3)}$$

Where:

NDA_{jt} is non-discretionary accrual for firm j in year t
A_{jt-1} is total assets for firm j in year t-1
ΔREV_{jt} is change in net revenue for firm j in year t
PPE_{jt} – is gross property, plant and equipment for firm j in year t
ΔREC_{jt} is change in accounts receivable for firm j in year t
β_0, β_1, β_2 is coefficients

The final step was to determine discretionary accruals by deducting non-discretionary accruals from total accruals as shown in equation 4

$$DA_{jt} = \frac{TA_{jt}}{A_{jt-1}} - \frac{NDA_{jt}}{A_{jt-1}} \text{ ---------- (4)}$$

4.2 Descriptive statistics

This statistic shows mean, maximum values, median, minimum values, skewness, standard deviation and kurtosis of all study variables. The Arithmetic mean is used to calculate average of any numerical data hence it measures central tendency employed to represent most classic values in value sets. Median is defined as middle item of all observations arranged in order. Median separates area of distribution into two parts that are equal. The standard deviation and variance are measures of distribution in the series. Kurtosis measures whether data are flat or peaked in comparative to normal dispersion. Skewness is an estimate of asymmetry of the dispersion of series around its mean (Triola, 2012).

The descriptive statistics aims to summarize and describe the features of the data. It has two methodologies one of them is the numerical method which measures and represents the median, mode, maximum, minimum and standard deviation (Triola, 2012). Focusing on numerical method, table 2 summarizes mean, minimum values, median, maximum values,

kurtosis, skewness and standard deviation for study variables from sample of 56 listed companies at NSE.

Table 2: Descriptive Statistics

	Discretionary Accruals	Board Composition	Remuneration Committee	Board Size	Board diversity
Mean	(0.0025)	0.7666	0.8081	0.9042	0.1406
Median	(0.0151)	0.8182	0.8000	0.9031	0.1250
Maximum	0.9385	1.0000	1.5000	1.1761	0.6667
Minimum	(0.7152)	0.0909	0.000	0.4771	0.000
Std. Dev.	0.1269	0.1698	0.2476	0.1385	0.1228
Skewness	1.5729	(1.7775)	(1.0603)	(0.6149)	0.6734
Kurtosis	15.5543	6.8912	6.2618	3.0566	3.4042
N	517	517	517	517	517

The results of table 2 reveal mean value of discretionary accruals for the companies is -0.0024 with a standard deviation of about 0.13. The value of mean average implies that earnings management practices in the listed firms, are taking downward direction (-0.0024) that is firms are practicing income decreasing earnings management. Firms could be engaging in cookie jar reserves activity which entails making more reserves in the current period so that lower earnings are reported. The positive kurtosis of earnings management implies its distribution measure is leptokurtic and data series has more values that are higher than the mean. The skewness for earnings management measures is positive implying the distribution

is skewed to the right.

For independent variables, the results as shown in Table 2 exhibit that mean average of board composition was 0.767 with minimum of 0.09, standard deviation of 0.17, maximum of 1, skewness of -1.77 which means data is negatively skewed. The distribution is leptokurtic as the value of kurtosis is greater than 3 which imply that, the series has more values which are higher than the mean. Remuneration committee independence mean average was 0.808 with maximum of 1.5, minimum of 0, standard deviation of 0.25, skewness of -1.06 which means data is negatively skewed and its leptokurtic as the value of kurtosis of 6.26 is >3 which implies that the series has more values that are higher than the mean. Board size had mean of 0.904 with maximum of 1.18, minimum of 0.48, standard deviation of 0.14, skewness of -0.61 which means data is negatively skewed and the value of kurtosis of 3.05. Board diversity had mean 0.14 with maximum of 0.67, minimum of 0.0, standard deviation of 0.12, skewness of 0.67 which means data is positively skewed and its leptokurtic as the value of kurtosis of 3.40 is >3 which implies that the series has more values which are higher than the mean.

4.3 Correlation analysis

Correlation analysis of study variables was done using Pearson's correlation coefficient. This was utilized to analyze degree of relationship between corporate governance and earnings management, between corporate governance, executive compensation and earnings management and between corporate governance, firm characteristics and earnings management. The values of Pearson correlation coefficient (r) ranges from +1 to -1. When association is not present between two variables r value is zero (0). When association is positive r value will be greater than zero (0) this implies, increase in value of one variable leads to an increase in value of another variable. Negative association is depicted by r value of less than zero (0), meaning an increase in value of one variable leads to a decrease in value of the other variable (Cooper & Schindler, 2014). The degree of relationship between corporate governance (board composition, board diversity, remuneration committee independence and board size) and earnings management (measured as discretionary accrual) was determined by computing the Pearson product coefficient value. The correlation of the variables is given in Table 3.

Table 3 reveals, there was negative correlation between earnings management and board composition (r = -0.084). Similarly, negative correlation exists between earnings management and board diversity (r = -0.079). Negative correlation also exists between board size and earnings management (r = -0.123). Contrary, there was positive correlation between earnings management and remuneration committee independence (r = 0.056).

Table 3: Correlation analysis

	DA	BCOM	BDIV	BREM	BSIZE
DA	1.000	(0.076)	(0.068)	0.061	(0.125)
BCOM		1.000	0.014	0.178	0.275
BDIV			1.000	(0.075)	0.325
BREM				1.000	0.121
BSIZE					1.000

4.4 Hypothesis Testing

The objective was to determine association between corporate governance and earnings management for companies listed at NSE. The study predicted that association between corporate governance and earnings management for companies listed at Nairobi Securities Exchange was not significant. Corporate governance comprised of board composition, independence of remuneration committee, board size and diversity. Earnings management was represented by discretionary accruals where modified Jones model was utilized for its computation. Multiple regression Model 5 was used to test the hypothesis and determine whether board composition, remuneration committee independence, board size and board

diversity significantly predicted discretionary accruals of companies listed at NSE in Kenya. The first null hypothesis was as follows:

Ho: Relationship between corporate governance and earnings management of companies listed at Nairobi Securities Exchange is not significant.

The results of regression model 5 is summarized in Table 4

$$DA_{jt} = \beta_{0\,jt} + \beta_1 BCOM_{jt} + \beta_2 RCOM_{jt} + \beta_3 BSIZE_{jt} + \beta_4 BDIV_{jt} + \varepsilon_{jt} \text{ ---------- (5)}$$

Table 4: Regression Result of Corporate Governance and Earnings Management

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.093015	0.041522	2.240131	0.0255
BCOM	-0.046204	0.034392	-1.343462	0.1797
BDIV	-0.026306	0.048153	-0.546297	0.5851
RCOM	0.043032	0.022929	1.876766	0.0611
BSIZE	-0.100827	0.044393	-2.271246	0.0235

R-squared	0.025473
Adjusted R-squared	0.017860
S.E. of regression	0.125744
Sum squared resid	8.095482
Log likelihood	340.9252
F-statistic	3.345824
Prob(F-statistic)	0.010174

Dependent Variable: DA
Method: Panel Least Squares
Periods included: 10
Cross-sections included: 56
Total panel (unbalanced) observations: 517

As per table 4, the relationship between board composition and discretionary accruals was negative with coefficient of -0.046 but not statistically significant as p value > 0.05. The

association between board diversity and earnings management was negative but not statistically significant with coefficient value of -0.026 and $p > 0.05$. In addition, there was a positive non-significant relationship between independence of remuneration committee and earnings management as p value > 0.05. From the corporate governance components only board size had significant negative influence on earnings management with $p < 0.05$. The overall model as per the p value of f statistics was statistically significant since p value was 0.01 which is less than 5%. This implies that board composition, board diversity, independence of remuneration committee and board size jointly influences earnings management of listed companies in Kenya. The linear regression model 5 was therefore presented as follows: $DA_{jt} = 0.093 - 0.04620BCOM_{jt} - 0.0263\ BDIV_{jt} + 0.0430RCOM_{jt} – 0.1008BSIZE_{jt.}$

From the results of Table 4 the overall model produced Adjusted R Squared of 0.018, F = 3.44, and p = 0.01. The results of the overall model reveal statistically significant relationship exists between earnings management and corporate governance. The Null hypothesis was therefore rejected implying that significant relationship exists between corporate governance and earnings management of companies listed at Nairobi securities Exchange.

5. Findings and Discussions

The study objective of study was to determine relationship between corporate governance and earnings management for companies listed at Nairobi Securities Exchange. The study hypothesized that relationship between corporate governance and earnings management was not significant. The null hypothesis was rejected implying that relationship between corporate governance and earnings management of companies listed at Nairobi Securities Exchange is significant.

The statistically non-significant effect of board composition on earnings management is consistent with studies by Gulzar and wang (2011); Abed et al. (2012); Nugroho and Eko (2011) whose findings revealed that there is no significant relationship between board independence and earnings management. These results contradict studies by Bekiris and Doukakis(2011) who looked into impact of corporate governance on earnings management and concluded that companies with high degree of corporate governance principles engaged less in earnings management practices. Waweru and Riro (2013); Iraya et al. (2015) who analyzed how corporate governance influenced earnings management concluded that high number of independent board members lowers earnings management practices. Enofe et al. (2017) whose finding revealed that when independence of board members is high earnings management is reduced. In Kenya, this study result could imply that as more emphasis has been placed on board independence, more companies have adhered to this requirement which has led to reduction in earnings management.

The negative statistically significant relationship between board size and earnings management results is harmonious with studies by Iraya et al.(2015) who analyzed how corporate governance influenced earnings management and concluded that when board size is large earnings management is low, Epps and Ismail (2009) whose findings indicated that firms with small board size engage in more earning management practices, Abed et al. (2012) analyzed relationship between corporate governance and earnings management and concluded that concluded that board size influences earnings management negatively. The results are contrary to studies by Peni and Vähämaa (2010) and Enofe et al.(2017) whose results revealed that there is significant positive relationship between board size and earnings management. It is also contrary to studies by Buniamin et al. (2012); Gulzar and Wang (2011) whose studies stated there is no significant relationship between board size and earnings management. From this study it was evident that board size has significant negative influence on earnings management implying that a large board size is good.

The non-significant negative relationship between board diversity and earnings management agrees with study by Hili and Affess (2012) who indicated women representation on board has no significant influence on earnings management. However, the results contradicts findings by Arun et al. (2015) study on presence of women directors on board influences earnings management revealed that higher number of women leads to decrease in earnings management. Gavious, et al. (2012) who analyzed relationship between female directors and earnings managements found that higher number of women on the board led to decrease in earnings management practices, Lakhal et al. (2015) who investigated the impact of women on earnings management and concluded that when women are chairs of the board or their number on the board is higher than men there is decrease in earnings management. Buniamin et al. (2012) whose study on effect of board diversity on discretionary accruals concluded that higher number of female members on board led to increase in earnings management practices. The non-statistically significance relationship of board diversity and earnings management can be due to low number of women as compared to men on board in most of listed companies in Kenya and, in some cases, it was zero. The results of this study and other empirical results reveal that there is need to put more emphasis in firms to appoint women on the board and more specific in Kenya to fulfil the two third gender rule in the board of directors.

The relationship between independence of remuneration committee on earnings management was not significant. These results are different from findings of studies by Epps and Ismail (2009) whose finding revealed that higher percentage of independence of remuneration committee results to an increase in earnings management practices and Liu et al. (2013) whose study revealed that influence of board and subcommittee on earnings management revealed that nominating/remunerating committee is negatively associated with earnings

management.

According to findings of Table 4 the relationship between corporate governance and earnings management reveal that board size is the only element that significantly influences earnings management. From this result it is important to have a standard on the appropriate size of board that will ensure quality of earnings since the current standard as given by CMA is general on the size of board (CMA, 2015_b). In Kenya as per the mean average of board composition (76.7%) as shown in Table 2 it is evident that most firms have adhered to the corporate governance guidelines that requires the board to consist of a minimum of 33% (1/3) of members who are independent (CMA, 2015_b).

The f statistics of the overall model as shown in Table 4 shows that its p value is significant. The first hypothesis was therefore rejected implying that relationship between corporate governance and earnings management of companies listed at Nairobi Securities Exchange is significant. This result is consistent with studies by Okougbo and Okike (2015) who concluded that corporate governance has an inverse relationship with earnings management

6. Conclusions and Recommendations

Rejection of null hypothesis implies that a significant relationship exists between corporate governance and earnings management. The only significant component was board size. On average listed companies have 76% of the board members being independent, 81% of the remuneration committee members being independent and board size averages 8. In addition, proportion of women on BOD is still very low averaging at 14% which is way lower than the proposed gender rule of 2/3. The negative significant relationship between board size and earnings management implies when board size is large, practices of earnings management is low. The significant association between corporate governance and earnings management therefore implies regulators of listed companies should emphasize the need to have large board sizes as a means of ensuring reduction in practices of earnings management.

The current study utilised modified Jones model for computing discretionary accruals. Future research could consider other models of computing discretionary accruals as this could give different results on earnings management practises. The researcher could also develop a model that has high precision of determining discretionary accruals in developing countries like Kenya. This study used companies listed at Nairobi Securities exchange as its context. Future studies could concentrate on companies that are not listed at securities market. This may be important especially because as per Kenyan guidelines on corporate governance it is a requirement for all companies whether listed or non-listed to comply to the guidelines.

July Vol4 No.2, 2020 PP 79- 95 ISSN 2522-3186

References

Abed, S., Al-Attar, A., & Suwaidan, M. (2012). Corporate governance and earnings management: Jordanian evidence. *International Business Research*, 5(1), 216-225

Arun, T. G., Almahrog, Y. E., & Aribi, Z. A. (2015). Female directors and earnings management: Evidence from UK companies. *International Review of Financial Analysis*, 39, 137-146.

Bekiris, F. V., & Doukakis, L.C. (2011). Corporate governance and accruals earnings management. *Managerial and Decision Economics*, 32(7), 439-456.

Buniamin, S., Johari, N. H., Rahman, N. R. A., & Rauf, F. H. A. (2012). Board diversity and discretionary accruals of the top 100 Malaysia corporate governance (MCG) index company. *African Journal of Business Management,* 6(29), 8496-8503.

Capital Markets Authority. (2015a). *The code of corporate governance practices for issuers of securities to the public 2015*. Gazette Notice No. 1420.

Capital Markets Authority. (2015b). CBK *and CMA joint press release-imperial bank in receivership.* Retrieved from http://www.cma.or.ke

Central Bank of Kenya. (2015). *Dubai bank Kenya Ltd under receivership*. Retrieved from http://www.centralbank.go.ke/press

Cooper, D. R., & Schindler, P. S. (2014). *Business Research Methods.(*12th Ed.). The McGraw− Hill Companies.

Dey, A. (2008). Corporate governance and agency conflicts. *Journal of Accounting Research*, 46(5), 1143-1181.

Enofe, A. O., Iyafekhe, C., & Eniola, J. O. (2017). Board ethnicity, gender diversity and earnings management: evidence from quoted firms in Nigeria. *International Journal of Economics, Commerce and Management*, 5(6), 78-90.

Epps, R. W., & Ismail, T. H. (2009). Board of directors' governance challenges and earnings management. *Journal of Accounting & Organizational Change*, 5(3), 390-416.

Gavious, I., Segev, E., & Yosef, R. (2012). Female directors and earnings management in high-technology firms. *Pacific Accounting Review*, *24*(1), 4-32.

González, J. S., & García-Meca, E. (2014). Does corporate governance influence earnings management in Latin American markets? *Journal of Business Ethics*, 121(3), 419-440.

Gulzar, M. A. & Wang, W. (2011). Corporate governance characteristics and earnings management: Empirical evidence from Chinese listed firms. *International Journal of Accounting and Financial Reporting*, 1(1), 133-151

Hili, W., & Affess, H. (2012). Corporate boards gender diversity and earnings persistence: The case of French listed firms. *Global Journal of Management and Business Research*, *12*(22).

Iraya, C., Mwangi, M., & Muchoki, G. W. (2015). Effect of corporate governance practices on earnings management of companies listed at the Nairobi Securities Exchange. *European Scientific Journal*, 11(1), 169-178.

Kalainathan, K., & Vijayarani, K. (2014). Block holder ownership structure of SriLankan listed companies. *International Journal of Research in Commerce and Management*, 5(8), 24-30

Kapoor, N., & Goel, S. (2017). Board characteristics, firm profitability and earnings management: Evidence from India. *Australian Accounting Review,* 27(2), 180-194.

Lakhal, F., Aguir, A., Lakhal, N., & Malek, A. (2015). Do women on boards and in top management reduce earnings management? Evidence in France. *Journal of Applied Business Research,* 31(3), 1107.

Larcker, D. F., Richardson, S. A., & Tuna, I. (2007). Corporate governance, accounting outcomes and organizational performance. *The accounting review,* 82(4), 963-1008.

Lasdi, L. (2013). The effect of information asymmetry on earnings management through accrual and real activities during global financial crisis. *Journal of Economics, Business and Accountancy Ventura,* 16(2), 325-338.

Latif, A. A. S., & Abdullah, F. (2015). The effectiveness of corporate governance in constraining earnings management in Pakistan. *Lahore Journal of Economics,* 20(1), 135-155

Liu, J., Harris, K., & Omar, N. (2013). Board committees and earnings management. *Corporate Board: Role, Duties and Composition*, 9(1), 6-17.

Norwani, N. M., Mohamed, Z. Z., & Chek, I. T. (2011). Corporate governance failure and its impact on financial reporting within selected companies. *International Journal of Business and Social Sciences*, 2(21), 205-213.

Nugroho, B., & Eko, U. (2011). Board characteristics and earnings management. *Journal of Administrative Science and Organization*, 18(1), 1-10.

Okougbo, P. O., & Okike, E. (2015). Corporate governance and earnings management: empirical evidence from Nigeria. *Corporate Ownership and Control,* 12 (4), 312-326.

Peni, E., & Vähämaa, S. (2010). Female executives and earnings management. *Managerial Finance*, 36(7),629-645

Sun, J., Liu, G., & Lan, G. (2011). Does female directorship on independent audit committees constrain earnings management? *Journal of Business Ethics*, 99(3), 369-382.

Triola, M, F. (2012). *Elementary Statistics (*12th edition). Addison - Wesley Pearson. USA

Uwuigbe, U., Ranti, U. O., & Okorie, B. (2015). Assessment of the effects of firms' characteristics on earnings management of listed firms in Nigeria. *Journal of Asian Economic and Financial Review,* 5(2), 218-228

Waweru, N. M., & Riro, G. K. (2013). Corporate governance, firm characteristics and earnings management in an emerging economy. *Journal of Applied Management Accounting Research*, 11(1), 43–64.

Yang, W. S., Chun, L. S., & Ramadili, S. M. (2009). The effect of board structure and institutional ownership structure on earnings management. *International Journal of Economics and Management,* 3(2), 332-353.